SMALL AND MINORITY BUSINESS IN THE DECADE OF THE 80's (PART 2)

HEARINGS
BEFORE THE
COMMITTEE ON SMALL BUSINESS
HOUSE OF REPRESENTATIVES
NINETY-SEVENTH CONGRESS
FIRST SESSION

PHOENIX, ARIZ., SEPTEMBER 1, 1981; AND
ATLANTA, GA., JANUARY 18, 1982

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SMALL AND MINORITY BUSINESS IN THE DECADE OF THE 80's (PART 2)

TUESDAY, SEPTEMBER 1, 1981

House of Representatives,
Committee on Small Business,
Phoenix, Ariz.

The committee met, pursuant to notice, at 9 a.m., in the hearing chamber of the county board of supervisors, Maricopa County Building, 205 West Jefferson Street, Phoenix, Ariz., Hon. Parren J. Mitchell (chairman of the committee) presiding.

OPENING STATEMENT OF CHAIRMAN MITCHELL

Mr. **Mitchell**. Good morning. This hearing will now come to order.

On behalf of my colleagues of the Small Business Committee of the House of Representatives, I welcome you to the third field hearing this committee will conduct throughout the United States.

In January of this year, I was elected to chair the Small Business Committee of the U.S. House of Representatives. One of my first actions was to institute a policy for this committee to conduct at least four field hearings throughout the country. There are two primary reasons for such policy. First, I have been in Congress for almost 10 years and during this period, I have heard excellent testimony from small business owners who were able to afford the cost of traveling to Washington. Far too often, however, many small business owners cannot afford the financial burden associated with testifying before Congress in Washington. As a result of this, my colleagues and I have not been privileged to hear the excellent ideas of the many small business entrepreneurs throughout this Nation. Second, hearings in Washington are necessary. Congress must be able to solicit information from the administration's policymakers on how they are implementing laws passed to benefit the citizenry. Throughout my 10 years in Congress, however, I have witnessed a void between the laws passed by Congress and the assistance actually received by the intended beneficiaries. Thus, field hearings are necessary to ascertain the effectiveness of the administration in carrying out the mandates of Congress.

The small and minority business community is the foundation of this Nation's economic system. More than 98 percent of the commercial establishments in the United States are small businesses. Indeed, there are nearly 14 million small businesses in this country. Unfortunately, data suggests the share of output being produced by small businesses has been declining. Small businesses generated 43 percent of the aggregate output in 1963, 40 percent in

1972, and approximately 39 percent in 1976. This represents a decline in small business output of approximately 0.3 percent annually. During the same period, large business increased its share of output by 2.4 percent representing an acceleration in its market share and aggregate output position. A large amount of evidence is available which supports a theory that this economic concentration results in inflationary overcharges amounting to approximately 9 percent of the gross national product. Small businesses are a victim of this process, but the biggest victim is the consumer.

Of parallel significance, the decline of productivity in the American economy is directly related to the decline in the small business sector. A National Science Foundation study reveals that small firms produced nearly 4 times as many innovations per research and development dollar than medium-sized firms and more than 24 times as many than the largest firms in the period between 1953 and 1973. Yet, instead of encouraging small business innovation, Federal procurement policy has stifled the incentives for innovation. Through the 1970's small business received less than 5 percent of the Federal research and development funds while the largest firms, which by all indicated research are less innovative, received more than 50 percent of Federal research and development dollars.

In view of these conditions, it is critical that the administration begin to foster policies which will support small and minority businesses. To date, the administration's overall economic recovery blueprint is void of what I consider to be necessary strong policy directions for small businesses and especially minority businesses.

Some may argue that most minority businesses in this country are small businesses and thus special assistance should not be given to minority businesses. Yes, the former businesses are experiencing many of the same problems as their majority counterparts. Unfortunately, however, racism and other barriers to the free enterprise system has placed a heavier burden on the development and maturity of minority businesses. It is for these reasons that in 1978, Congress passed Public Law 95-507. This law is designed to assist and to foster the development of socially and economically disadvantaged businesses. Public Law 95-507 recognizes that these businesses are not presently capable of competing with their majority counterparts, and therefore procurement, management, and technical assistance must be provided if the free enterprise system is to truly work for all Americans. In this regard, the 8(a) program was developed as a part of Public Law 95-507 to provide minority businesses with procurement and other business development assistance.

The 8(a) program has been the subject of extensive congressional review and criticism since its administrative conception in 1968 and statutory formulation in 1978. On May 1, 1981, Mr. Cardenas, Administrator of the Small Business Administration [SBA], announced new tough policies for the 8(a) program. A moratorium was placed on the admission of new 8(a) firms; 8(a) contracts with a value of $2 million or more must be approved by Mr. Cardenas. Advance payment and business development expense approval requirements have also been restructured. Also, on May 1, 1981, Mr. Cardenas authorized an immediate size standard review of all 8(a) firms alleged to be above SBA's definition of small businesses. Program termination procedures will be activated for 8(a) firms found to be above these standards. It is my understanding that SBA has recently completed the first stage of this review and 20 firms out of a total of 48 reviewed have been found to be large businesses. I understand further that many of these 20 firms are appealing SBA's initial findings.

Let me say I find it appalling that the SBA is going ahead with a graduation program particularly in light of the fact that the House Small Business Committee, and the Congress, had indicated to many that no such program could be promulgated until such time as it was reviewed by the House Small Business Committee.

In addition to the above, on June 1, 1981, Mr. Cardenas had published in the Federal Register proposed 8(a) graduation regulations pursuant to Public Law 96-481. If implemented, these regulations will limit an 8(a) firm's participation in the 8(a) program to a 3- to 5-year period.

On July 7, 1981, this committee conducted its first field hearing in Los Angeles, Calif. The second hearing was on July 18, 1981, in Chicago, Ill. Witnesses from both hearings provided the committee with excellent testimony. Some of the general problem areas discussed were high interest rates, SBA's uncertain new role in its guaranteed loan program, and the inability of participating banks to loan money with a 70-percent guarantee, underutilization of minority business firms as subcontractors by prime contractors as required by Public Law 95-507, and the failure of SBA and procuring agencies to comply fully with the requirements of the 8(a) program.

Today's hearing will focus on a cross section of problems and opportunities affecting the small and minority business community. Since January of this year, the administration has proposed a new economic recovery program, small and minority business program changes, deep agency budget cuts, and business tax cuts. In view of this, I believe it is imperative that the Congress and especially this committee, which I am proud to chair, begin a systematic investigation of the impact of such broad new policy directions on the small and minority business sector of this Nation's economy and on the ability of the Federal agencies to implement the laws of this land.

Witnesses appearing before us today will speak on these issues and on other issues affecting the survival of the small and minority business community. I am confident that at the conclusion of this hearing, we will have a better understanding of how policy decisions made in Washington are impacting the bedrock of this Nation, the small and minority business community.

That concludes my opening statement.

At this point, Congressman Addabbo, who has been a long-term friend of small business, and minority business, is unable to be with us, but he asked that his opening statement be submitted for the record.

OPENING STATEMENT OF HON. JOSEPH P. ADDABBO, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF NEW YORK

Mr. **Addabbo**. Mr. Chairman, I regret that I was not able to participate in this valuable hearing personally. As a result, I ask that this written statement be submitted for the record.

First, please allow me to commend you for continuing your aggressive steps in seeking out the views of the public, especially from areas not ordinarily heard from, either because the businesses are not close enough to Washington, or because they cannot afford to have high priced lobbyists represent them.

Second, I would like to note that one of our witnesses, Mr. Tom Trimboli, is not unknown to the House Small Business Committee. Before he became SBA Phoenix District Director, Tom was counsel to our committee. He contributed immeasurably to the development of many of the small business programs which he now so ably administers at SBA. True to form, I understand that Tom assisted the committee in bringing this hearing to Phoenix, and I thank him and his staff for their help.

Finally, I would like to thank the witnesses who took time out of their busy schedules to express their views on small business and small disadvantaged business development. I look forward to reading the testimony submitted at this hearing, since we are faced with a number of serious obstacles to the goal of all small and disadvantaged businesses entrance into America's economic mainstream.

Thank you.

Mr. **Mitchell**. I am delighted to have with us this morning Congressman Hatcher, a very fine member of the committee who represents the Second District of Georgia. I am very, very pleased you can be with us. If you have an opening statement, we would be glad to hear it at this time.

Mr. **Hatcher**. Mr. Chairman, I would just like to commend you for scheduling these hearings. I think it will be very helpful to the committee in considering legislation. I look forward to hearing from our witnesses here today.

Mr. **Mitchell**. Thank you very much for being with us. In addition, Congressman John Rhodes was unable to participate in the hearing, but he too has prepared an opening statement for the hearing today. Without objection, I will submit his opening statement for the record.

OPENING STATEMENT OF HON. JOHN J. RHODES, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF ARIZONA

Mr. **Rhodes**. Mr. Chairman and members of the Committee on Small Business, it is a pleasure for me to welcome the committee to Phoenix as it continues its field hearings on the problems facing the small business community. Arizona, the Phoenix metropolitan area in particular, has been one of the country's fastest developing regions for a number of years now. As a result, we have an increasing number of small businesses in Arizona that have been exposed to the multitude of problems confronting the Nation's small business community. I am sure they welcome this opportunity to present their views to the committee.

I am particularly pleased that Chairman Mitchell is here to conduct these hearings. Parren and I have been friends for many years and although we disagree on some matters, we are in full agreement in the matter of helping those in the small business community and that small business is the backbone of the American economy.

Because the vitality of small business is so essential to our economy, it is imperative that Congress and the administration pursue policies which will mitigate excessive regulatory and tax burdens, which are particular impediments to small businesses.

In this regard, I am pleased to see that the administration is conducting a comprehensive review of the current maze of Federal regulations and their impact on individuals and businesses. Similarly, I would hope that this committee will exercise its oversight responsibilities and pursue needed legislative reforms.

It is also pertinent to note that Congress was not unmindful of small business needs when it passed the Tax Incentive Act earlier this summer. Among some of the provisions particularly important to small business, and which I supported, were accelerated depreciation, tax bracket reductions, and changes in estate and gift taxes. The changes in estate taxation increase the exemption from $175,000 to $600,000 by 1987 and completely eliminate estate taxes on bequests made to spouses. Such reforms will go a long way toward holding family businesses together.

These recent efforts of Congress and the administration to support small business are welcome, of course. However, much remains to be done in this area, and I commend you, Mr. Chairman, and your committee, for your continued commitment to the needs of America's small businesses.

Mr. MITCHELL. We have broken our hearing down into several panels. Our leadoff witness this morning is Mr. Thomas Trimboli, the District Director for the SBA Phoenix office. Mr. Trimboli and I are old friends. He was on the staff of the House Small Business Committee. If there ever was an advocate for small business, and minority business, Tom Trimboli has been that advocate. I am very pleased you can be with us.

TESTIMONY OF THOMAS TRIMBOLI, PHOENIX DISTRICT DIRECTOR, SMALL BUSINESS ADMINISTRATION

Mr. TRIMBOLI. Thank you very much, Mr. Chairman. I appreciate that.

I do have a prepared statement, Mr. Chairman. At your discretion, I would either read that or submit it for the record and summarize it.

Mr. MITCHELL. I think it would be entirely up to you. I have no strong feelings one way or another. What I am going to suggest for all the witnesses who have submitted statements, is that they have an option. They can either read their statement in its entirety or merely submit it for the record. Which do you prefer to do?

Mr. TRIMBOLI. Thank you, Mr. Chairman. I would like to submit the prepared statement on behalf of the agency and summarize, if I may.

Mr. MITCHELL. Without objection, your entire prepared statement is submitted for the record.

Mr. **Trimboli**. Thank you, Mr. Chairman.

Before I get into the various programs and activities of the Small Business Administration in Arizona, I think it necessary that I give a brief description of the economy of the State.

Our local economy is really dominated by two phenomena. There is extreme rapid growth of business in this area; between 1972 and 1977 the number of businesses in the State grew by over 44 percent. In addition to that, most of our businesses are small businesses. Under our SBA definitions of small business—of the 46,547 businesses that the Bureau of Census says we have in this State, 46,337 have under 250 employees. So you can see about 99 percent of our businesses, if not better, would qualify as small businesses.

Our industrial base is basically service and retail; 60 percent of our businesses are in that category. If we add construction to that total, these three industrial areas would account for about 70 percent of the businesses in the State.

Manufacturing over recent years has made rather substantial gains. I would think that light manufacturing is where the future of the State's economy may well lie.

Between 1972 and 1977 the number of our manufacturers increased by 48 percent. Gross receipts increased from $4 billion to over $7 billion. This was in a period of just 5 years. Yet according to most recent statistics we can gather on employment, the typical manufacturer only employs 47 employees. So once again even in this area we are in every sense a small business State.

With respect to minority business, Mr. Chairman, Mr. Hatcher, minority businesses in the State account for about 10 percent of the businesses. But the rate of growth of minority business is not as great as the growth of majority businesses. We estimate between 1972 and 1977 the rate of growth of minority businesses in the State was only 28 percent. Nationally the number of all minority businesses during that period increased by 30.7 percent. As I indicated, all business in Arizona grew by 44 percent. So minority business is lagging behind the majority business in terms of growth. As a result of that, the percentage of market share going to minority business in this State I believe is decreasing.

As you know, in the Small Business Administration we manage a variety of different programs and activities. I suppose we are best known for the financial assistance programs we have. We have attached to our prepared statement a number of appendixes which include program statistics in these areas.

But I think you might find it of more interest if I told you where our money is going, what types of businesses are profiting from our money.

We did an analysis recently based upon the standard industrial code of our loan recipients, based on minority code, because we wanted to see where the money was going and who was benefiting. Based upon that study, we have certain conclusions which begin on page 3 of my prepared statement. If I may, I would like to read those.

In fiscal year 1980, the Phoenix District Office made or guaranteed 284 loans having a gross dollar amount of $32.7 million. More than 51 percent of this loan amount went to the service and retail industries. The type of business receiving the largest percent of our dollars was found in the retail industry, eating places, which captured 10 percent of the total dollars. The second major recipient was in service, auto repair shops, which received a 3-percent share. However, manufacturing and wholesaling showed unanticipated strength, with manufacturing receiving 26 percent and wholesaling 11 percent of the total dollars.

Wholesale is growing quite rapidly here, also.

In fiscal year 1980, with respect to minority business, we guaranteed 43 loans for a gross value of $4,205,059—SBA share was $3.96 million—to minority owned businesses. This represents only 13 percent of all loan dollars and 15 percent of the number of loans. Over 73 percent of the minority loan volume went to minority businesses in service and retail industries. You can see from our appendix, Mr. Chairman, that the dollar amount of loans going to minority business has been on the decline in recent years. It was only this year that we managed to reverse that trend.

In the first 9 months of this fiscal year, we have actually exceeded last year's total dollar amount of loans to minority business; we had exceeded what we did all of last year in the first 9 months of this year.

But I think of extreme importance, too, is where the money is going in the minority community. We all talk about the minority community predominating in service and retail types of business. According to our study we found we actually lent to businesses that were spread across 139 different standard industrial codes. However, when we look at the minority business that year, we see only 31 of those SIC's with minority business loan activity.

We found that in 11 standard industrial codes, in 11 areas, the only loan activity was minority business. And in five other SIC's minority business activity accounted for more than 50 percent but less than 100 percent of the loan activity.

From that you can see, Mr. Chairman, minority businesses are gravitating toward business areas where there is a distinct lack of activity from the majority business community. It is a phenomenon that we did not know existed. We did know most of the money was going to service and retail minority businesses, but we had no idea it was that concentrated within service and retail. We had no idea in certain standard industrial codes, the only activity we would find would be minority business.

With the exception of manufacturing, we found that the distribution of our loan dollars across industrial areas was fairly consistent with the population of businesses in the State.

As I indicated previously, Mr. Chairman, so far in this fiscal year I believe our loan activity, which is recited in our first attachment, indicates that we have done $4.1 million in minority business activity, and that our total loan activity in the first 9 months is $26.7 million. In all of last year our SBA share of loans was about $30 million. And this year we anticipate coming very close to $40 million. We anticipate increasing our programs by 30 percent in this fiscal year over last year. So there has been a tremendous increase, even with prime at the high level it is at.

I would like to tell the committee also about some things that we have done to try to reverse the downward trend, and I think has been successful in reversing the downward trend of loan activity for minority business. We have received substantial support from our Regional Administrator, Mr. Robert Strauss in particular, to engage in what I consider to be rather unconventional, innovative type of financing. We engaged in a program effort with the blessing of Mr. Strauss that we call the tandem loan program. What we try to address here is the problem we find most often in our direct loan program where as you know we put the money out into the business community, the minority business community, and we put it out in $40,000 chunks, $50,000 chunks. We really do not do that much to ameliorate the condition of that community, to promote the mobility from the service and retail business to a type of business that is perhaps more lucrative, more job intensive, more important to the State's economy.

To try to address this problem, we made a marriage between our guarantee and direct loan programs. The way this would work is that under certain qualifying situations we have informed our participating banks we will make a direct loan immediately behind a guaranteed loan. In this particular example we cite in the prepared statement, we had an applicant that came to us, a black businessman, who wanted to establish a drugstore in Scottsdale. We do not have many minority businesses in Scottsdale. We do not have many blacks that own drugstores in the State that I know of. He needed $250,000 to get started; but he could not afford $250,000 at 22½ percent. He could not afford to go to a bank and borrow that much money at that high rate. But it was a good deal. We think the man can succeed.

So we worked with the bank. We said to the bank, if you lend $150,000 to that small businessman, we will guarantee the loan. But we will also lend on our own through our direct loan program $100,000; we will lend that $100,000 at 9¼ percent, and we will subordinate to the bank. So in effect to the bank we appeared to be something very close to equity. In fact, to the bank we are equity. To the minority business person we provided $250,000 worth of financing at an average cost of money substantially less than 22½ percent. We helped create bank relations between a minority business person and a bank, which our direct loan program as you know does not do. We got a minority business person into an industrial area that is devoid of minority business participation. And we have him in a geographical area that is underrepresented in terms of minority-owned business.

So that has worked well. That is the first case we have done. We have two or three more in the works.

The effect of the increased interest rates on direct loans, Mr. Chairman, may slow the progress in this particular program, though. Because we were putting the direct money out at 9¼. As you know, now the direct interest rate is at 15 percent. So that will increase the average cost of money and might slow down this type of effort.

I really do believe that we should try to engage in more creative type of financings along these lines to meet the changing circumstances, the rapidly changing circumstances in the economy.

One of the major problems we are finding, of course, is the lack of equity, especially in the minority business community. Because of lack of equity we find minority businesses gravitating toward those industrial areas that have the lowest entrance barriers. They are the areas with the highest competition. They are the industrial areas with the lowest probability for success. Until the equity capital problem is addressed I am afraid most of our efforts, regardless of how creative they may be, will fall pretty short of the mark. There is no substitute for equity, ownership money. I know you and Mr. Addabbo last year sponsored a bill to address that problem. And I do really believe that problem does need addressing.

With respect to other general types of problems in the financial area, the extremely high interest rates we are facing are causing severe problems, not only for those small businesses that are trying to seek financing, but also for small businesses that already have variable rate financings from the banks. As you know, these loans can be adjusted, the interest rates can be adjusted quarterly. We may have approved a very good loan at 15 or 16 percent; but at 22 or 23 percent it becomes a troubled loan. So we do have a problem with the existing loan clients, with variable rate loans, because the prime is as high as it is.

Mr. MITCHELL. May I interrupt you just a minute. Generally I try to let the witness get all the way through. But under your bank participation loan program, do you operate under the variable rate?

Mr. TRIMBOLI. Most of the loans coming in, Mr. Chairman, are variable rate loans.

Mr. MITCHELL. Well, that means that small business, or minority business, or both, getting a bank participation loan, might be paying as much as 22, 23 percent; is that correct?

Mr. TRIMBOLI. Yes, Mr. Chairman. The new loans coming in with the present regulations that are on the books can be 2¼, 2¾ above the prime. So the new loans coming in are coming in at 22, 23 percent.

What I am addressing here also is loans we may have made a year or so ago, that may have been lower interest rate loans when initially made but they have been adjusted upward.

Mr. MITCHELL. I understood where you were. That is why I had to interrupt you. Because I was concerned that we are going to compound the problem area.

Under the new loans coming in, if we are up to 23 percent, the margin is not that big.

Mr. TRIMBOLI. It is extremely heavy debt service. I heard one bank in this State quote a report from a major brokerage house located in New York City. According to this brokerage house, it is estimated that for nonfinancial types of businesses in the United States today, 40 percent of every cash flow dollar goes to service debt. That is a tremendous portion of the money coming into any business. Forty percent of every dollar goes to service debt according to this one study. Of course we see this very heavy debt service for these loans coming in at such high interest rates. And that is a problem. And it would be a lie for me to represent to this committee that it was not a problem, because it is. I see what is happening to our people out there.

In addition to that, two more things with our loan programs I would like to address before going on.

We think that the $500,000 maximum amount on the SBA guaranteed portion of the loan is too small. It is too small today to accommodate the legitimate financial needs of small businesses. The $500,000 in many cases just cannot give us the latitude to address the total financial needs for small business, especially a medium sized small business that might need some capital for plant expansion, for working capital, to meet payrolls. A bank likes to put all this together in a package. Our present limit really works to the disadvantage of the small businesses that would need to go shopping around to various banks for all its financial needs. The $500,000 we have found has worked to the detriment of some of our business people.

And of course, as the committee knows, size standards that we are operating under presently are desperately in need of revision. The administration in Washington I believe has that matter under review. I understand something may be coming out on that within the short term. But inflation has eroded the validity of many of our size standards that are based upon gross receipts, especially industry that deals with petroleum products, which would be a prime example. The profit margin may be a couple of mills on a cent, yet gross receipts may be in the millions and millions. So we think to improve the efficiency of our program those standards would have to be revised.

Management assistance is another primary functional area we have in the office. The backbone of the management assistance delivery system is the SCORE program. We find our employees are basically in a position of managing resources available to the office, those resources being SCORE, Small Business Institutes and the 7(j) program. It is of extreme necessity, though, that we get out into the community more. We will be doing this beginning with the next fiscal year. We must work more with the chambers of commerce and local organizations, local trade groups, so that they perhaps can provide one-on-one counseling, so that perhaps they can join with us in cosponsoring workshops and training seminars.

It is extremely important, though, that when we do this activity that we deviate a bit I think from the traditional path. By deviation I mean we should really be in a position to go into the community, assess the needs of that local community, not use some pat formula, some pat curriculum that has been used for a number of years and just keep on using it because it has been used for a number of years. We should go into the community, address local needs, make the curriculum really relevant to the people we are trying to help. We also have to devise a method of procedure to go back to the people after the assistance is provided and give them an opportunity to criticize us, give them an opportunity to say how their expectations were or were not met by the training that we provided.

So in summary, we have to work more with the community here, we have to try to leverage our resources far better, we have to assess the needs of the local community better, and tailor our training courses to the needs of the local community and provide the mechanism that will allow for the expeditious review and feedback of how well we are performing in the field.

In addition to management assistance we operate the 8(a) program in this district. I am sure the committee is fully aware of the changes, both the changes that have been enacted and the proposed changes that Administrator Cardenas has proposed, with respect to the program.

I will not take up the committee's time to reiterate those changes.

I would like to say a little bit about what the Phoenix office is doing with this program.

If you look at our statistics, you can readily conclude it was not too many years ago that this program was fairly dormant in this district. As I indicated, 10 percent of our businesses are minority owned, 30 percent of our population is minority. Yet we only have a handful of businesses, 24 businesses in the portfolio. In one of the attachments to the prepared statement, attachment 3, we see as recently as fiscal year 1978 only $2.8 million went through this program in terms of contracts. Last year, fiscal year 1980, $6 million went through the program. This year, Mr. Chairman, I believe that we will do somewhere between $12 million and $15 million. So I believe we will double our performance over last year.

That doubling was not the result of gratuitous circumstances. We had to work on the doubling. We had to actively go out and sell this program to the Federal buying establishment. We had to indicate to them we were committed to the program; not only committed to the program because it was statute, but committed to the program because we believed in the program. We also made it known that we were very, very serious about it, and that there were rules and regulations governing the program, the defense acquisition regulations, Federal procurement regulations, and that we would hold the agencies accountable to those regulations.

We have aggressively marketed these firms with something fairly simple and had tremendous results. We took every one of the firms and profiled them, listed their key employees, machinery, their equipment, their bonding line, bank references, business references. We did an 8½ by 11 sheet on each one of the 8(a) firms, put it together in a booklet. We sent it out to every buying activity, Federal buying activity in the State and to prime contractors. From that rather simple effort we have managed to receive numerous inquiries from Federal agencies. We have picked up contracts as a result of that very simple effort. Agencies coming back to us and saying, "we did not know you had anybody that can do that." And of course, we have heard that story before. But now everybody has this set of profiles.

We also sent that out to major prime contractors, private sector firms. I regret the response from the private sector has not been as spontaneous or as broad as the response from the Federal sector.

So we have done that type of activity. We have marketed these firms. The way I am approaching the 8(a) program from a management standpoint, Mr. Chairman, when I say from a management standpoint I mean managing my internal resources in the office I try to take the program and visualize it in three separate types of functions. I look at the most basic functions, I would call that area perhaps the technical area. I would look at those functions as being the technical hands-on skills that my people need to find contracts, to negotiate contracts, to understand what the Federal procurement law is all about, to explain to my subcontractors, my 8(a) firms, what it means when one signs an 8(a) contract. As you know when one signs a Federal contract a whole series of laws and regulations come into play. The Government, of course, presumes when you sign this you know all about those regulations and statutes you have just bound yourself to. So the first part of managing this program is what I would call the technical functions, the hands-on skills and training people to keep up on the skills.

The second part of the program, which I consider the major part of the program activity, should be what I call the developmental stage. It is that stage where my employees are able to assess, No. 1, what makes this firm economically disadvantaged, how do I make that determination, what does a nondisadvantaged firm in this particular industrial area, in this State of Arizona look like, where is my firm deficient? No. 2, and most importantly, what do I have to do to try to correct that? We should come up with a plan of action for every deficiency noted. No. 3, when we come up with a plan of action we should be in a relatively good position to estimate the time it will take to achieve the corrective action which needs to be taken. The major thrust of the program should be, I believe, in this developmental stage.

The third stage in the program I would label as being the transitional stage. To be honest with you, Mr. Chairman, we have not gotten to that stage yet. That transitional stage is a stage where we take the more matured 8(a) firms and try to establish a bridge between them and the established community, with prime contractors. As you know, the section 211 subcontracting program can work very well there. We should try to enter into agreements with State and local governments and with prime contractors, that would say, for example, that we have seasoned firms here, we are committed to these firms, and we will provide these firms with resources that they need—if you, on the other hand, will come back and promise to us that you will do something special to try to qualify these firms to be vendors to your business. That this should be an agreement there, a quid pro quo. This transitional stage, of course, is the last stage in the 8(a) process. And I think we are deficient in that stage. I hope to work on that come next fiscal year. But I think if I had to say where most of the activity should focus, it should be in that developmental stage and in that transitional stage. In the technical stage I think we are talking basically about a one-time effort to make sure our people have the skills that they need, and make sure those skills are updated. But I think most of the program activity should really focus on the other two stages.

Procurement, to get to our last subject area, is another major program area with our district. We do handle most of the procurement programs. Major activity centers on subcontracting, however. We do find a problem, Mr. Chairman, in the administration of that program. The problem we find is that in some instances we may cite a firm for noncompliance, and we may go through our procedures to call that fact to the attention of higher authority. But it seems to us at least in this State, and I do not know about the rest of the country, that the Government has failed to take any sanction against any contractor that has been found in noncompliance. We have found an attitude among some that a law very good on its face may have all the teeth that Congress has given it, that the Federal Government has failed to use the teeth and has failed to bite down, so to speak. It has conveyed the impression in some quarters that one can violate the law with impunity.

Not only do we find that situation, but a more frequent situation we find is that in a number of instances contracts are being awarded still, today, that do not contain the requisite subcontracting plan required by statute. Federal buying agencies are still awarding these contracts without the plans. We find that situation to be more frequent than finding violators of the plans. We find a more frequent situation that the plan is not in there, than we find the prime contractors violating the plans.

Mr. Chairman, I can see by the expression on your face you have some questions to ask on that.

With that statement, I will conclude my remarks.

[Mr. Trimboli's prepared statement and attachments follow:]

PREPARED STATEMENT OF THOMAS TRIMBOLI, DISTRICT DIRECTOR, PHOENIX DISTRICT OFFICE, SMALL BUSINESS ADMINISTRATION

Mr. Chairman, and Members of the Committee, I am appreciative of the opportunity to appear before you today to speak about the developmental needs of small and small disadvantaged businesses in the State of Arizona.

Before I discuss the various SBA programs and activities, I believe it necessary to briefly describe our local economy.

A review of the Arizona economy clearly shows that it is dominated by two significant phenomena: rapid growth and an extremely high concentration of small businesses.

According to U.S. Census data, in 1972, there was a total of 32,249 businesses in the State. Of this number, 32,050 had 250 employees or less. By 1977, there were 46,547 businesses—a net increase of 44.3 percent in 5 years. Of these 46,547, better than 99 percent or 46,337 had 250 employees or less.

While the State's economy is heavily dependent upon service and retail types of businesses (about 60 percent of our businesses are so classified), the growth pattern has virtually left no industrial category untouched. Manufacturing, in particular, is enjoying a position of constantly increased importance to the State. During the 1972-1977 period, the number of manufacturers increased by 48 percent and gross receipts climbed from $4.0 billion to over $7.1 billion. However, according to the most recent employment statistics available, in 1978 the typical Arizona manufacturer employed only 47 employees. One can rightly conclude that Arizona is, in every sense, a small business State.

According to the latest U.S. Census data available, minority-owned businesses have not grown as fast as the overall Arizona economy. Arizona business grew by over 44 percent in the 1972-1977 period, but the number of minority businesses grew by only 28 percent. Nationally, the number of minority firms grew by 30.7 percent during this period.

Thus, we have in this State a rapidly expanding small business economy. We also have a State in which the rate of growth of minority businesses appears to lag behind the growth rate of the Arizona economy as a whole.

FINANCIAL PROGRAMS

The loan volume of this district office is attached to this statement and marked as attachment 1.

Of more significance than the absolute amount of loans and its increasing trend over time, is a review of those types of industrial establishments which benefit from the SBA financial assistance programs in Arizona.

Recently, this office completed a study of its fiscal year 1980 loan volume (both direct and guaranteed) by Standard Industrial Code (SIC) of the client small business and by the ethnic/racial status of the business owners. Our study resulted in the following findings:

(a) In fiscal year 1980, the Phoenix District Office made or guaranteed 284 loans having a gross dollar amount of $32.7 million. More than 51 percent of this loan amount went to the service and retail industries. The type of business receiving the largest percent of our dollars was found in the retail industry, eating places, which captured 10 percent of the total dollars. The second major recipient was in service, auto repair shops, which received a 3 percent share. However, manufacturing and wholesaling showed unanticipated strength with manufacturing receiving 26 percent and wholesaling 11 percent of the total dollars.

(b) In fiscal year 1980, the Phoenix District Office made or guaranteed 43 loans for a gross value of $4,205,059 (SBA share was $3.96 million) to minority-owned businesses. This represents only 13 percent of all loan dollars and 15 percent of the number of loans. Over 73 percent of the minority loan volume went to minority businesses in service and retail industries.

(c) While we provided financial assistance to businesses spread over 139 different industrial areas, minority business was found in only 31 SICs (65 percent of which were in service or retail). However, of perhaps more interest is the fact that in 11 SICs, the only loan activity was with minority business, and in five other SICs minority business activity accounted for more than 50 percent (but less than 100 percent) of all loan dollars made to those SICs.

(d) With the exception of manufacturing, the distribution of our loan dollars is fairly consistent with the industrial distribution of business in the Arizona economy.

In fiscal year 1978, the SBA share of loans to minority businesses totalled $5.05 million—in fiscal year 1979, $4.63 million, and in fiscal year 1980, the minority business amount decreased to $3.96 million.

This office is making a deliberate and purposeful effort to reverse this trend. We are marketing our programs and devising some innovative approaches to better service this constituency.

One program effort which we have initiated in Phoenix with the concurrence of our Regional Administrator, Robert Strauss, is a tandem loan program. We have advised all of our participating bank lenders that SBA will, in certain instances, approve simultaneously both a guarantee and a direct loan to the same minority business borrower. The first tandem loan made by this office was approved in late July of this year. In that situation, a minority entrepreneur wanted to start a drug store in Scottsdale. The total project cost was $250,000. The client could not afford a $250,000 bank guarantee loan at 22¾ percent. SBA, therefore, made a $100,000 direct loan at 9¼ percent and the bank made a $150,000 loan through our guarantee program. The effective cost of money to the borrower was substantially reduced; we helped to establish a bank relationship between the client and the lender and we now have a minority-owned business in an industrial category in which minorities, in this State, are almost totally under-represented. We believe this more creative use of direct loan funds can and will be of extreme benefit. Other similar efforts are needed.

These actions appear to be meeting with success. For the first 9 months (three fiscal quarters) of this year, our total loan volume of both direct and guarantee loans (SBA share) was $26.78 million. Of that amount, minority-owned businesses received $4.12 million or 15.38 percent.

However, as evidenced by our SIC study, unless the equity problems of minority business are addressed, all of our efforts in providing some affordable debt capital will be of limited benefit. Because of the lack of ownership capital—equity—minority entrepreneurs gravitate toward businesses with the lowest entrance barriers, the highest competition and the lowest probability of success. It is my expectation that progress in the penetration of more lucrative industrial areas by minority-owned concerns will be extremely limited. While creative SBA lending practices can help, it cannot, in any sense, replace the need for ownership capital.

There are other issues which are more pervasive in scope and which are adversely affecting our entire small business community. One primary concern in the financial assistance area is the extremely high cost of debt capital. In this area, the President's economic recovery program has been designed to lower the rate of inflation, reduce the size of the Federal deficit, and enable interest rates to come down.

Another problem we have experienced with our guarantee program is directly caused by inflation. In 1976 Congress enacted Public Law 94-305 which raised SBA's guarantee loan limit from $350,000 to $500,000. Needless to say, because of inflation, $500,000 in 1981 does not have the same value as $500,000 in 1976. In this District, SBA is unable in many instances to be helpful because the total capital needs exceed our statutory maximum.

For example, small businesses (especially those having large payrolls) desire a banking relationship which can provide for their entire financial needs. A single small business may have need for a revolving credit line, term financing for working capital, equipment, and construction for plant expansion. A bank may be reluctant to participate with SBA (and, therefore, service total client needs) because our existing $500,000 loan limit cannot accommodate a package request for its small business customer.

Finally, inflation has also called into question the validity of those size standards which are based on gross receipts. Efforts presently underway in this Administration to adjust and revise such standards are desperately needed if we are to continue to service the truly small business person.

MANAGEMENT ASSISTANCE

Management capability is a prerequisite to economic development. Since productive resources are limited, it is imperative that such resources be managed in a manner best calculated not only to produce salable goods and services but also to provide an adequate return on investment to the business owners.

SBA does have a variety of tools to deliver management assistance to the small business community. SCORE is presently the backbone of our delivery system. Small Business Institutes and call-contractors are, in addition, used by this District Office. However, these resources cannot be utilized on a very broad scale due to both funding limitation and time restraints. In addition, our office has presently employed three Business Management Specialists and an Assistant District Director for Management Assistance. Consequently, we are not staffed to provide direct one-on-one counseling to all small business clients seeking our assistance. It is necessary, therefore, that our management assistance personnel be primarily concerned with both the wise management of internal resources available to the office and with the leveraging of potential management assistance resources found in the local community.

In the Phoenix District Office we have undertaken steps to better manage our available, internal management resources. We have, for example, profiled the type of client that should be served by each of our available resources. In addition, we have devised a system in cooperation with SCORE that assigns a SCORE volunteer to each direct loan applicant. That volunteer stays with the applicant throughout the processing, closing, disbursement, and servicing of the loan. Each participating volunteer, therefore, establishes a portfolio of SBA direct loan recipients which he/she provides assistance to throughout the life of a loan. We plan to undertake similar initiatives dealing with other program areas in the future.

However, of primary concern is the leveraging of outside resources to provide one-on-one counseling. In this regard, we will be working more closely with Chambers of Commerce, professional and trade organizations, and educational institutions to devise more counseling programs for our small business constituency.

With respect to training activities such as workshops or seminars, we plan to concentrate on business areas of priority concern to the local community and to tailor our training to fit the needs of the locale. This will involve increasing the number of local organizations that will cosponsor training activities; devising relevant curricula; obtaining good instructors and formulating a system of review and feedback so that we may assess the value of our assistance and correct the deficiencies.

Statistics relating to our present activity are in attachment 2.

8(A) PROGRAM

One of the first tasks undertaken by the Administrator, Michael Cardenas, was to examine the 8(a) program and the criticisms leveled against it and establish a policy to make the program work more effectively. The new policies announced are:

(1) All 8(a) firms must be small by SBA size standards.

(2) Administrator Cardenas published in the Federal Register on June 1 a proposed rule establishing a maximum term to be negotiated between SBA and program participants, with a maximum term of 3 years for service firms and 5 years for other types of firms. The purpose of the 8(a) program is to help small businesses develop their potential and become a viable concern. This opportunity cannot be provided to others if some businesses are allowed to remain in the program indefinitely.

(3) New applications are being held temporarily in abeyance for the 8(a) program until a procedure can be developed to comply with Section 106 of Public Law 96-481. Implementing this section establishes the basis on which the graduation of a firm is determined. When these procedures are implemented, including training on SBA field personnel, the moratorium will be lifted.

(4) Regional Administrators may approve the expenditure of Business Development Expense funds up to 15 percent or $50,000 on a single 8(a) subcontract. Any amount in excess of these figures will require approval of the Central Office.

(5) The authorization level in the use of advance payments for Regional Administrators will be restricted to 40 percent or $100,000 on a single contractor. If the advance payments run in excess of this amount it must then be approved by our Central Office. In addition, the use of an advance payment on more than one 8(a) subcontract by a client at a time must be approved by the SBA's Washington Office.

These broad policy changes and positive steps should enable a greater number of eligible small disadvantaged firms to participate in this program.

In the Phoenix District Office we have undertaken activity designed to promote the competitiveness of our 24 participating firms. We have conducted formal meetings with all of our 8(a) concerns, both for training purposes and to explain the intricacies of SBA's regulatory requirements for program participation. We have aggressively marketed the program with Federal buying activities. We have developed profiles of each of our 8(a) firms and disseminated this information throughout the State—not only to Government procurement centers but also to large prime contractors in order to assist with some non-8(a) marketing.

I believe that our efforts have produced good results. We expect that our 8(a) awards this year will double over last year's total. Our 8(a) statistics are recited in attachment 3.

PROCUREMENT

The Phoenix District Office has a Procurement Division responsible for the conduct of procurement programs authorized by the Small Business Act. Procurement volume for the Phoenix District Office is shown on Attachment 4.

These activities include providing small firms information pertaining to what our various Federal buying centers purchase and by providing guidance on how to get on various bidders' lists. In addition, we are responsible for the operations of the Set-Aside and Certificate of Competency Programs. Our major activity, however, does concern itself with the execution of the Subcontracting Program mandated by Public Law 95-507. We are, however, experiencing problems in the administration of this program. The major problems are reporting, goal setting and the imposition of sanctions in the event of non-compliance with either plans or the requirement to have plans.

Presently, SBA maintains the Procurement Automated Source System, which we believe is the best and most accurate list of small and small minority businesses in the Federal Government. But, the Department of Commerce also maintains a listing of minority businesses, and private organizations funded in part by the Department of Commerce maintain additional lists. Moreover, there are numerous local directories and even more directories maintained by large prime contractors. Needless to say, this duplication of effort is expensive, confusing and wasteful. We believe that the PASS should be the source list for small and small minority business and that duplicative efforts funded by the Federal Government should be terminated.

The administration of the Subcontracting Program is difficult, in some instances, due to the failure of the Federal Government to impose sanctions on prime contractors.

A mechanism needs to be devised to expeditiously resolve cases on non-compliance or illegal contract awards. Our subcontracting efforts will become, in large part, meaningless if violators have the perception that one can break the law with impunity.

Mr. Chairman, this complets my prepared statement and I will, of course, respond to any questions the Committee may have.

ATTACHMENT 1.—LENDING ACTIVITY, PHOENIX DISTRICT, SBA SHARE ONLY, BY CATEGORY

[Dollars in thousands]

	9 mos. through June 30, 1981	Fiscal year		
		1980	1979	1978
Guaranty	$22,317	$24,360	$23,848	$19,378
Number	160	215	170	186
Direct	$4,467	$5,327	$5,826	$3,931
Number	71	69	102	77
Minority	$4,121	$3,955	$4,627	$5,051
Number	48	43	64	71

ATTACHMENT 1.—LENDING ACTIVITY, PHOENIX DISTRICT, SBA SHARE ONLY, BY CATEGORY—Continued

[Dollars in thousands]

	9 mos. through June 30, 1981	Fiscal year		
		1980	1979	1978
Women	$2,130	NR	NR	NR
Number	41	NR	NR	NR
Number of mini loans	23	NR	NR	NR

NR: No records prior to fiscal year 1981.

ATTACHMENT 2.—PHOENIX DISTRICT OFFICE MANAGEMENT ASSISTANCE

	9 mos. through June 30, 1981	Fiscal year 1980
Counseling:		
Total	2,024	2,612
Minority	228	336
Women	599	677
Training:		
Total	4,967	5,945
Minority	554	662
Women	2,551	2667

ATTACHMENT 3.—PHOENIX DISTRICT OFFICE 8(a) PROGRAM STATISTICS

[August 10, 1981]

	Number of firms in program	Number of contracts per year	Dollar amount of contracts
Fiscal year 1978	19	20	2,831,872
Fiscal year 1979	24	38	4,729,677
Fiscal year 1980	24	46	6,023,217
Fiscal year 1981 to date	24	16	5,186,623

Contract proposals and negotiations in process—$4,562,209.

ATTACHMENT 4.—PROCUREMENT AWARD DATA, PHOENIX DISTRICT OFFICE

PRIME CONTRACT PROGRAM [1]

[Dollars in thousands]

	Total awards	Small business	Percent	Set-aside	Percent
Fiscal year 1978	$104,000	$40,000	39	$18,000	17
Fiscal year 1979	150,000	56,000	37	18,000	12
Fiscal year 1980	183,000	66,000	36	25,000	14
Fiscal year 1981 through June 30	124,000	44,000	36	17,000	14

SUBCONTRACT PROGRAM [1]

[Dollars in thousands]

	Total awards	Small business	Percent	Minority awards	Percent
Fiscal year 1978	$144,000	$79,000	55	$3,000	2
Fiscal year 1979	188,000	111,000	59	5,000	3
Fiscal year 1980	235,000	124,000	53	6,000	3

SUBCONTRACT PROGRAM [1]—Continued

[Dollars in thousands]

	Total awards	Small business	Percent	Minority awards	Percent
Fiscal year 1981 through June 30	$155,000	$86,000	56	$5,000	3

[1] The data above are not inclusive of all Federal procurement actions in the State of Arizona but reflect only those awards reported in subcontracting programs in Arizona.

Mr. MITCHELL. Thank you. That is a very insightful and incisive statement. Of course I have questions, particularly on the latter part of your testimony.

Am I understanding you correctly to say that there are instances in which Public Law 95-507 has been violated, and you have forwarded to the attention of someone these violations and no action has taken place?

Mr. TRIMBOLI. We have seen no action take place. We have done that. We have seen no action take place as a result of those referrals.

Mr. MITCHELL. About how many such referrals?

Mr. TRIMBOLI. Mr. Chairman, I could give you the statistics—this year, I believe the statistics are recent through the second quarter. This would cover a 6-month period of time.

We have found 53 cases where we have gone out and we have found the contractor to be in compliance with the plans in the contract 53 cases. We have found two cases where the contractor in our estimation was not in compliance with the plans, two violations. We have found 22 instances when we found contracts that did not have plans, but in our opinion under statute are required to have plans.

Mr. MITCHELL. To whom did you submit data with reference to the two violations?

Mr. TRIMBOLI. With respect to the two violations, with respect to the 22 no-plans, we submit that of course to our region. Region informs, I believe, the contract administration agency of our findings; region does also inform the contractor of our findings. We have found region to be quite expeditious in responding to our reports. Region then takes this information——

Mr. MITCHELL. Then the fault is not at the regional level. You feel it is somewhere else?

Mr. TRIMBOLI. Yes, sir.

Mr. MITCHELL. I certainly want to dig into that. I am certain Mr. Hatcher would be interested, also. We cannot have a scofflaw public. As I mentioned last night, the President was very firm with the controllers who went on strike. He said, "What else can I do but terminate them, they have violated the law." If you have two instances of clearcut violation, and 22 instances where they were simply in noncompliance, we should not permit that to happen. As long as the law is on the books, it must be obeyed. We will be digging into that.

As per usual, you come up with some tremendously innovative ideas. I like that idea about the tandem plan, where SBA makes the direct loan and also a guaranteed bank loan as a single package. That seems to have a great potential. Can you think of any other ways in which SBA could make better use of its program resources? For example, have you given any consideration to a loan program whereby small business obtained a loan similar to the present SBA guaranteed bank loan and SBA provided not only the guarantee but also interest on subsidy, in light of that enormous 23 percent? Is that workable?

Mr. TRIMBOLI. It has been suggested by some people in the community, Mr. Chairman, that perhaps the SBA in view of these very high interest rates use some of its direct loan money or perhaps some other money that might be appropriated by the Congress——

Mr. MITCHELL. Not likely.

Mr. TRIMBOLI. But use some of these resources to defray the high interest rate that is being charged on bank guaranteed loans. Represent, for example, to the bank, that we will pick up any interest expense that might be over a certain amount that is set by the Congress, 15, 16 percent perhaps, that SBA might pick up an interest rate higher than that. The small business person would pay up to that amount. I think that is creative.

Mr. MITCHELL. Certainly worth exploring.

Mr. TRIMBOLI. I think it is worth exploring.

Mr. MITCHELL. I have many more questions. You have been up here for almost three-quarters of an hour. I want to get one more in. Then I will turn to Mr. Hatcher.

The central office in Washington imposed a moratorium on 8(a) certification. It came up with some new regulations with regard to advance payments, business development expenses. I think they all have to be cleared in Washington now. They also came up with some new regulations on graduation. At what point, if at any point, were you and the regional office consulted in terms of these rather dramatic new changes?

Mr. TRIMBOLI. I cannot speak for the regional office. With respect to the district office, we found out about the changes when they were effective. We got a memorandum telling us of the changes.

Mr. MITCHELL. Then, at the district level, there was no consultation with you or your counterparts, as far as you know, with reference to the impact of these changes on the way your operations were running?

Mr. TRIMBOLI. There was no consultation with the Phoenix district office, no.

Mr. MITCHELL. Last, what was the impact? Suddenly you were notified, no new 8(a) certifications. Suddenly you were told no more advance payments, except clearance in Washington. Did that facilitate the operation of the district office?

Mr. TRIMBOLI. We are at the stage in the district office where we are just getting into the program the way it should be run, to be honest with you. We have not yet availed ourselves of advance payments. Most of our contractors are construction contractors.

Mr. MITCHELL. What about the moratorium?

Mr. TRIMBOLI. The moratorium, as I understand it, has precluded us from accepting applications. That has impacted our ability to accept applications for program participation. We have 24 firms in the portfolio. This year I think we will double volume over last year. Between $12 million and $15 million this year. We have our contractors fairly well loaded up with 8(a) work. Because of that, we have had to turn away some 8(a) work.

Mr. **Mitchell**. Will you be around most of the day?

Mr. **Trimboli**. Yes.

Mr. **Mitchell**. I am glad that you will be. I have some more questions I really would like to ask you later on. I do not want to keep you too long. In the event that we cannot get back to you, I would like to put those questions in writing to you. For example, I would like to know if you are satisfied with the quality of the 8(a) contracts offered by the agencies. A whole series of questions like that.

Thank you very much.

Mr. Hatcher.

Mr. **Hatcher**. Thank you, sir.

Where do you place the fault for the breakdown of the imposition of sanctions on prime contractors—within SBA, at the national level, within other agencies of Government, departments, or Justice Department, or where?

Mr. **Trimboli**. Well, Mr. Hatcher, rather than fix blame, I would rather say what I believe should be done. First of all I think what has to be done is that a system must be devised to expeditiously resolve these cases of noncompliance. There must be something in place—whether that be a mechanism that is formulated by an interagency agreement between this agency and buying agencies of the Government, whether it comes out of the Office of Federal Procurement Policy, whether it comes out of the White House, out of OMB, there should be a mechanism in place that we can have ready resort to in order to present a case. And there should be, I believe, a series of sanctions that are agreed upon so that when a resolution is made that there is violation, we do not have to worry about what types of sanctions are going to be applied, because they will already have been predetermined.

There is a lack of, I think, initiative to create this mechanism. And if I have to place fault, the fault is in not having the mechanism. Who should establish that, I leave to others in Washington.

Mr. **Hatcher**. Thank you. That is all I have, Mr. Chairman.

Mr. **Mitchell**. Thank you very much, Mr. Trimboli.

Our next witness is Mr. Malcolm Straus, chairman of the Small Business Advisory Council. Thank you for taking time from what is always a very busy day for you to be with us. We appreciate it.

We received a copy of your statement. I have had an opportunity to read it. You have the same option as Mr. Trimboli. You can present your statement in its entirety, or submit it for the record and merely speak to the highlights. Which do you prefer?

TESTIMONY OF MALCOLM STRAUS, CHAIRMAN, SMALL BUSINESS ADVISORY COUNCIL, ACCOMPANIED BY JOE ACOSTA AND RUBEN ESTRADA

Mr. **Straus**. Mr. Chairman, I would like to read my statement into the record.

I would like to introduce two members of the Arizona Advisory Council here with me today, not only to give me moral support, but to help me field questions that I may not be able to answer. On my right is Mr. Joe Acosta, and on my left, Mr. Ruben Estrada. These gentlemen have served on the Arizona Advisory Council for many years.

Mr. MITCHELL. I have had the pleasure of meeting both of those gentlemen. We welcome you here.

Before presenting your testimony, I think the explanation must be made about this fascinating bola that I am wearing. It was given to me last night at an affair. I was on the platform. I said it was so beautiful I would wear it to this hearing. There it is. I hope the television cameras focus in on it frequently, because it is quite a nice gift.

Mr. Straus.

Mr. STRAUS. Thank you.

Mr. Chairman and members of the committee, I appreciate this opportunity to appear before you today and to share the views of the advisory council regarding the developmental needs of Arizona's small and small disadvantaged business community. As you are aware, the Small Business Advisory Council is comprised of business and professional people from throughout the State. We meet periodically to discuss issues of importance to small business and to recommend actions that SBA may take to better fulfill its mission.

At our most recent meeting, we discussed issues we thought of particular concern to this committee, and this statement represents the consensus of our views.

Before I proceed, however, I believe it necessary to inform this committee about our local economy. We are in every sense a small business State—all but a few hundred Arizona firms meet the SBA definition of small business. We are strongly based in the service and retail industries which provide most of our jobs and our business gross receipts. Consequently, any prolonged downward trend in the economy would have severe repercussions in this State—since service and retail firms are, generally, most susceptible to adverse economic conditions. During our recent council meeting, therefore, it was no surprise that capital formation issues constituted our first topic of interest.

Capital formation among small business has been seriously affected by inflation, soaring interest rates, and the restricted availability of equity capital. Small business, in addition, is hard pressed to meet the rising cost of other factors of production aside from capital such as escalating labor and energy costs.

The present tax system does not provide small business with the opportunity to generate needed capital from internal operations. Therefore, resort to traditional lending sources has become a routine necessity. Small firms, however, have been, historically, unable to compete with larger firms for access to debt capital. When interest rates increase dramatically—a condition that has persisted since last January—fewer small businesses meet credit standards, and those that do find capital more expensive than their larger counterparts. This condition has precluded many small firms from raising debt capital from external sources. Expansion—and in many cases, survival— becomes impossible.

For those firms that can qualify for credit in this market, a disproportionate amount of resources is spent servicing debt. In fact, one estimate we have heard is that for nonfinancial types of businesses in the United States today, 40 percent of every cash flow dollar goes to service debt. If this increased cost of doing business is passed on to the consumer, inflation is the result; if it cannot be passed on, the businessman must absorb this increased cost, which can jeopardize its existence, since the margin for errors in business judgment becomes negligible.

In order to remedy these problems, we believe it necessary that tax measures and other legislative or administrative measures be targeted to encourage both capital investment and retention in small business, and to reduce the cost of debt capital.

With respect to reducing the costs of debt capital, we would suggest several changes to the SBA guarantee lending program.

Initially, we wish to commend this committee for recent legislation it has sponsored which provides for extending the term of existing SBA guarantee loans upon the payment of a 1-percent fee by the borrower. We believe this step will provide some relief because longer maturities should result in lower monthly loan payments.

We are, however, very much concerned by a proposed regulation recently promulgated by SBA which would limit the maximum allowable interest rate on guaranteed loans to low New York prime—that is, the elimination of the 2¼- to 2¾-percent spread over prime presently permissible. At first blush, it may appear that this was intended to lower the cost of capital to the borrower. However, its effect, we believe, will be to convert the problem of cost of capital to one of the availability of capital—a much more dangerous situation. Yield is a function of risk, and if SBA lowers the permissible yield on its guarantee loans, the lower the risk a financial institution will be willing to take. This will result in a substantial decrease in guarantee loan volume since banks have ample demand for their product without the necessity of participating with SBA at interest rates less than that which are obtainable in the open market.

We suggest, in the alternative, expansion and duplication of a test program now being conducted by the Phoenix district office. The tandem loan program, as it is entitled, is directed at minority businesses which are unable to obtain financial assistance under the agency's guaranteed loan program in amounts sufficient to meet their specific needs. Under certain guidelines, the SBA will approve both a direct loan and a guaranteed loan at their respective interest rates to the same borrower. Since the interest rate on direct loans is substantially less, the overall cost of money to the borrower is effectively reduced through the combination of the two interest rates. Tandem loans give minority businesses the opportunity to establish relationships with banks which a direct loan, by itself, will not promote. It also allows for larger deals which otherwise would not be funded. A further benefit is that the resources of the direct loan program are maximized through leveraging so that the Government gets the biggest play for its dollar.

Other changes which will, we believe, result in lower costs of debt capital to the borrower involve modification to the Internal Revenue Code.

We would propose that Congress permit lenders a total or partial tax exclusion from income for those revenues generated from an SBA guaranteed loan, provided that the lender reduces its interest rates on these small business loans to some predetermined level acceptable to the Congress. This, we believe, would encourage more affordable debt and help the small business person recapture some of its own tax dollars paid to the Government.

Another approach using the Federal taxation system would allow the small business guarantee loan borrower a total or partial tax credit for interest paid on its loan. Since many small firms pay taxes quarterly, this proposal would result in an easing of cash flow and, therefore, result in those same benefits to small business described in our tax exclusion recommendation.

Thus far we have been discussing recommendations that would result in a reduction in the cost of debt capital. However, we believe it imperative to mention that many business people in our State face the problem of availability as opposed to the cost of capital. These disadvantaged persons, who are primarily racial and ethnic minorities, desperately need relief.

Under the terms of the old economic opportunity loan program, we are advised that SBA could have legally given a 100-percent guarantee on loans made to the disadvantaged, but that the agency chose, administratively, to limit the full guarantee only to 8(a) firms. We know of the recent change to the law which consolidates all loan programs, and it is our impression that Congress has not limited by law the 100-percent guarantee to 8(a) firms. If that is so, we would recommend that SBA be allowed and directed by new legislation to aggressively pursue a 100-percent guarantee program not only for 8(a) firms but for all racial and ethnic minority business people and other disadvantaged persons who have a good chance for succeeding in the business world. Once again, if the yield to the banks on these loans is to stay constant, or possibly decreased, the risk to the lending institution must decrease accordingly if more volume is desired.

As mentioned previously, small business also has a pressing need for equity capital. There is little incentive today for most investors to take equity positions in small business. Banks are paying about 18 percent on certificates of deposit, and U.S. Treasury notes are yielding 14 to 15 percent. Such high yields encourage risk aversion and, consequently, adversely impact the small business seeking equity.

In order to encourage investors to take the risks associated with small business equity financings, we believe that the tax structure should be amended. We understand that this committee is promoting legislative change which would establish a capital gains rollover. This change, we understand, would permit an investor to defer income realized from the sale or exchange of a small business equity instrument, provided that the gain is reinvested in another small business equity security within a given time frame. The advisory council fully supports this legislative initiative.

In addition, however, we would propose that investors—other than large business—be allowed either a partial or full tax credit for their small business equity investments. The provision could be further limited to those small businesses, to be defined by the Congress, which are best able to produce employment opportunities or other desired economic results such as locating in underdeveloped or rural areas. Such an incentive would be certain to produce the equity that small business needs for its growth.

Aside from these specific recommendations which pertain to the needs of small business for affordable debt capital and equity, other measures can be taken to assist in capital formation.

It is our understanding that a bill is presently pending in the U.S. Senate which would create a hybrid security instrument called a small business participating debenture. This debenture would be issued by a small business and would be exempt from SEC registration and disclosure requirement. The instrument would carry a very nominal interest rate—3 percent—but would also contain a formula for the pro rata share of profits to be allocated between the investors and one of the owners. Distributions to the investor are taxed at a favorable capital gains rate and deductible as an expense by the business owner. In addition, the owner does not have to give up part of his/her business to raise needed capital.

We support this proposed legislation since we believe it will result in increased investments in small business. However, we would suggest that the Congress also consider giving SBA the authority to purchase participating debentures either in addition to, or in lieu of, the proposal presented in the Senate bill.

Our last recommendation in the capital formation area is another proposed change to the Internal Revenue Code which would provide for nontaxable profit retention. In other words, some or all of the profit generated by a small business should be exempted from taxation provided that it is reinvested or plowed back into the business in a manner that will either create jobs or result in the acquisition of fixed assets. While the Government would forgo some immediate tax gain, the reinvestment in the small business would promote competition, increase employment, and spur greater productivity. In the long run, such efforts would expand the economy and result in increased revenues to the U.S. Treasury.

While small business was given considerable assistance by passage of Public Law 95-507, they continue to face obstacles in obtaining their fair share of Federal contracts.

One of the major problem areas centers on the administration of the subcontracting program mandated by Public Law 95-507. The Federal Government is simply not imposing sanctions for the noncompliance of prime contractors, and in other cases is still awarding contracts without the required subcontracting plan. Although lack of compliance may be grounds for termination for default, it does not appear that the Government has yet imposed any sanctions in cases of noncompliance. We believe the subcontracting provisions of Public Law 95-507 to be fundamentally sound and desperately needed by the small and small disadvantaged business community. We fail to understand why mismanagement has been tolerated and why the Government has delayed active program execution so as to thwart congressional interest.

We would urge that a clear and certain policy be implemented to expeditiously remedy noncompliance cases and those instances where contracting officers make awards without the statutorily required plans. Once an effective Federal policy and procedure is implemented in this regard, participation in the subcontracting program by small and disadvantaged small business will, we are certain, greatly increase.

The advisory council fully supports the 8(a) program and its statutory purpose to generate competitive minority-owned small business firms through the use of the Federal procurement system. We feel there is an ample statutory base for the accomplishment of this objective in the enabling legislation and do not support amending legislation or regulations which would curtail the ability of minority-owned enterprises to achieve this stated goal. The council is concerned that the program should not be used simply as a medium to channel contracts to minority-owned business, and feels that the proposed wholesale regulatory reform that would do this in the name of curing program abuses is ill-advised. We propose that the statutory intent would best be met by vigorous program administration in the field and a carefully drafted set of criteria for program participation designed to promote the competitiveness and, therefore, the business development goals of participating 8(a) concerns.

Effective management is vital to the development and growth of small business. For this reason, the delivery of management assistance to the small business community is of great concern to the council. We recognize that current Federal resources in this area are extremely limited and, therefore, it becomes imperative that these resources are leveraged to result in maximum service to the community. In addition, the management assistance programs of SBA should be tailored to meet the particularized needs of the local small business constituency. Resources of the agency could be utilized most efficiently through the expanded use of local community organizations to provide individualized counseling to small business clients. The management assistance program should also strive to address current local problems through its workshops and should devise some indicia measuring the success and relevancy of those workshops for the small business community through feedback and suggestions from participants. Succinctly stated, we believe that SBA should continue its activity to work in concert with local organizations and to increase its flexibility to tailor training courses to the needs of the community.

We understand that much debate has occurred recently with respect to minority enterprise programs. The council, therefore, elected to present its views on this issue. It is the consensus of the advisory council that minority small business persons do suffer from disadvantages that are not common to all small business people, generally, and that these disadvantages are a result of racial and ethnic discrimination. Affirmative efforts are necessary to ameliorate these conditions. We, therefore, support such efforts and agree with the Congress that our intended goal should be the creation and expansion of competitive minority-owned firms. We urge, therefore, that the administration maintain the efforts commenced in this area and that adherence to this intended goal be afforded the priority of concern it rightly deserves.

Mr. Chairman, that completes my testimony. We will of course answer any questions the committee may have.

Mr. MITCHELL. Thank you very much, Mr. Straus. It was just excellent testimony.

It is interesting that you focus in on some of the same problem areas as Mr. Trimboli, which means we are really prioritizing the issues that this committee ought to be addressing.

The CHAIRMAN. Before putting some questions to you, I am very pleased to see that Congressman Eldon Rudd is here. Almost all of you know him. He represents the Fourth District of Arizona. I am glad that you could take time to visit us at least for a few moments this morning. I know a little bit about your schedule for today. Is it eight other engagements you have, or seven? Anyway. Thank you for being here. If you would like to make a brief statement at this time, we would welcome it.

TESTIMONY OF HON. ELDON RUDD, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF ARIZONA

Mr. RUDD. Thank you, Mr. Chairman. I cannot tell you how delighted I am that you have taken the trouble with your committee to come to Phoenix, Ariz. Obviously the welcome that you have received and the interest that you have generated is apparent by the attendance here. I do very much wish to express my appreciation to you. I would like to submit a prepared statement for the record, with your permission.

Mr. MITCHELL. Without objection, the prepared statement will be submitted in its entirety for the record.

[Representative Rudd's prepared statement follows:]

PREPARED STATEMENT OF HON. ELDON RUDD, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF ARIZONA

It is a pleasure for me to be here today to address this field hearing of the Small Business Committee. I would like to take this opportunity to commend you, Mr. Chairman, for scheduling a hearing in Phoenix on this important subject.

George Gilder, in his best-selling book, "Wealth and Poverty," points out how crucial the function of entrepreneurship is in our system of free enterprise. He points out further the predominant role played by small businesses in performing this entrepreneurial function by sensing new market opportunities, responding to them and consequently creating many new jobs.

In truth, small businesses are the very heart of our economic system. Without them, we could not possibly achieve the continuous stream of new ideas which is the principal source of creativity and change in the economy.

It is important, therefore, for those of us who are in government to make sure that the laws and regulations we write do not inhibit small businesses in performing their necessary economic function. According to one estimate, the cost of complying with government regulations comes to $3,600 per year for every small business in America.

In recognition of the fact that small businesses are often less able than large corporations to comply with burdensome Federal regulations, Congress in 1980 passed the Regulatory Flexibility Act to promote a two-tiered system of regulatory activity. Congress should devote itself to overseeing the implementation of this act, so that it is fully respected by the agencies mandated to make regulations less burdensome on small businesses.

In addition, Congress should proceed with a comprehensive program of regulatory reform, which would effect a reduction in paperwork and a simplification of administrative procedure for all businesses. Such comprehensive legislation, together with the Reagan Administration's continuing review of the need for particular regulations, would make it possible for businesses, both small and large, to devote full attention to their first priority, providing quality goods and services at a reasonable cost.

Finally, it is obvious that general economic conditions play an important role in the success or failure of small businesses. High interest rates hit them especially hard, since the Federal government and large corporations have the financial leverage to claim available credit resources in a time of scarcity.

It is my opinion that the Reagan Administration's program for economic recovery offers the best hope for encouraging economic growth while restraining inflation and bringing interest rates down. The recently passed tax bill, in particular, will reduce the tax burden on small businesses and simplify their depreciation of capital assets.

In conclusion, let me reaffirm that small businesses are—and ought to be regarded as—the most vital part of our economic system. They do not ask for favoritism from government, only for a fair chance to compete in the marketplace. We should do everything in our power to make sure they have it.

Mr. RUDD. Your field hearings here have generated a lot of interest. As we discussed in Washington—as I indicated, my seven appointments I have, two of which I have taken this morning already, were scheduled long in advance. I am sorry I could not be here to support you. I also want to compliment you on the beautiful bola tie you have, because that is the official tie of our State of Arizona. It becomes you very well. Your reputation for conduct, dress, and demeanor is well known in Congress. Again, I appreciate that.

I am pleased that this meeting is taking place, because it really is not the giant corporations who provide or maintain prosperity for our Nation. It is the individual, the entrepreneur, the citizen, who invests, who devises, and who perceives the needs of our Nation across the land. And it is through the hard work of these individuals who really have faith in themselves, and vision for the future, and have confidence in their own abilities, and careful attention to costs, that provide the growth of economy in our country. It also generates prosperity—especially when we look at the fact that 80 percent or more—I am not on your committee, but speaking in general terms, if you will permit that—80 percent or more of our economy is made up or part of the small business, so-called small business operation. And those small businesses do succeed because they are willing to work hard, again, and to challenge the giants.

For example, we have many examples of the giants that have been outdistanced by the small business, the individual—Eastman Co. is one good example. We have someone who was willing to take a look at the Polaroid camera, and now become one of the giants. But all of these will fall into the category of what I think and choose to call capitalism—that is, respect for the individual and his ability to fulfill the needs of our Nation.

I could cite any number of examples. I will not do that. I think there is a great change in the offing. Make no mistake—the American people ordered that change. I am looking forward, as I know you are, to see what the effects are going to be. I think Congress must make certain in its legislation that it does not inhibit the economic function of the small business people who do generate the best in our economy, that Congress must proceed with regulatory reform, to reduce Government requirements, and simplification of administration procedures, and that Congress should find ways to reduce interest rates. That sounds a little trite, because we know we have to do that. But it is Congress that must find a way to do that. And all of the small businesses across the Nation deserve and all they ask for is a chance to compete. And we have got to make sure they have that opportunity.

Mr. Chairman, I do again appreciate your permitting me to sit up here with you. I know that this will be a highly successful field venture for this committee. I will be looking forward supporting you in ways that I can in Washington to carry forward the goals that I am sure we will have in the future for small business. Again, thank you very much. I appreciate the opportunity to be with you.

Mr. MITCHELL. Thank you for your statement. We are very pleased you are here. You can stay with us as long as your schedule will permit.

Mr. Straus, you indicated in your testimony that there was a need for a 100-percent guarantee program for non-8(a) minority businesses. I think we really do not need any new laws for that, or any major changes, because under the Budget Reconciliation Act that was just passed, it is quite possible now for SBA to guarantee up to 100 percent. What the law says is that for all loans of $100,000 or under, the law requires at least a 90-percent guarantee. That law does not preclude a 100-percent guarantee. It really is within the discretion of SBA. I think we need to convey that to the SBA. But I do not think we need any new legislation on that. That is one of the recommendations that could be acted on very swiftly. And I think it is an excellent recommendation.

You have some concern about noncompliance with Public Law 95-507. As I listened to your testimony, I heard you suggest that an effective procedure could be implemented to insure subcontracting compliance.

Can you suggest or recommend any specific changes which can be made in the current procedure which insure subcontracting compliance with Public Law 95-507?

Mr. STRAUS. I cannot think of any.

Joe?

Mr. ACOSTA. I think as Mr. Trimboli said earlier, apparently we need some action.

Mr. MITCHELL. Yes. He suggested perhaps an interagency sort of a board with sanctions already determined before the violations occur, so you do not have to sort out what sanctions should be applied to this case or that case. You would have some criteria established.

I will not tautologize the discussion at this point. But if you can come up with any further recommendations—it is ironic I have to put this question to you—but if you can come up with some further recommendations as to how you can make people comply with the law, I would appreciate it if you would send those recommendations to me.

Also in your testimony, Mr. Straus, when you were talking about minority business development, you stated that the proposed regulatory reform is ill-advised. Were you referring to the SBA's rulemaking for the forced graduation of firms? What particularly did you have in mind?

Mr. STRAUS. Let me try to find that.

Mr. MITCHELL. I think it is toward the very end of your testimony.

> We feel there is an ample statutory base for the accomplishment of this objective in the enabling legislation and do not support amending legislation or regulations which would curtail the ability of minority owned enterprises to achieve this goal.

There is another reference to it. But what I was concerned about—maybe I can pinpoint it for you. Do you support the proposed graduation of 8(a) firms that has been proposed by the Small Business Administration?

Mr. **Straus**. The current change?

Mr. **Mitchell**. Yes.

Mr. **Straus**. I believe the counsel expressed the view that they did not.

Mr. **Mitchell**. That is my understanding.

Let me ask you one other question. I am trying to figure out how to ask it properly.

We have had testimony to the effect that the forced graduation of 8(a) firms, No. 1, is in contradiction of SBA's own studies that says it takes almost 10 to 20 years before a firm can become truly viable, can compete in the open market, or sell public stock. We have also had testimony before this committee to the effect that if the present 8(a) firms are forced out of the program prematurely, they will not have access to capital in the regular money markets, they will not be able to deal with all of the institutionalized patterns and practices that exist, and that therefore because of these two factors those firms that are graduated, forced out of the program, will probably fold up in a year or two or three. Would you agree with that latter statement?

Mr. **Straus**. I cannot disagree with it. It depends. In other words, if they have had enough of the 8(a) work over the years, and they were able to build a good credit rating and establish themselves, certainly they will survive. If they were dependent upon 8(a) work entirely, the chance of their not surviving would be imminent, I would say.

It would seem to me, Mr. Chairman, that if they were prematurely graduated, if they did not fold and go under, that at best they would never grow. The whole thought of graduation of 8(a) contractors when there are 24 in the State of Arizona seems premature, since we do not have any contractors to graduate. We have only got 24. And we are talking about graduating them, instead of providing more assistance.

Mr. **Mitchell**. Let me put one other question to all three of you gentlemen.

In these proposed new changes, Mr. Cardenas has suggested that a firm remain in the 8(a) program no longer than 3 to 5 years. You have had experience with businesses, how long it takes them to grow, what is needed for growth. Is that 3- to 5-year period reasonable, in your opinion? Is that a prudent kind of approach?

Mr. **Acosta**. I do not know how the SBA arrived at 3 to 5 years. Working with a lot of small businesses, it does take at least 8 years to really develop and maybe longer to be able to develop into a business of any size, even within the small business.

Mr. **Mitchell**. Then the 3- to 5-year period is not an appropriate time frame.

Mr. **Acosta**. That is right.

Mr. **Estrada**. Mr. Chairman, the businesses that fail, 99 percent of them fail within the first 3 to 5 years. It would seem to me that is just too short a time to start graduation.

Mr. **Straus**. It would not be realistic.

Mr. **Mitchell**. Thank you, sir.

Congressman Hatcher.

Mr. **Hatcher**. No questions.

Mr. **Mitchell**. Gentlemen, thank you very much.

Let me point out we do not have members of the committee representing the minority side. And so we will ask the counsel for the minority side to submit some questions.

Mr. **Centner**. I appreciate being referred to as the minority side in these hearings, Mr. Chairman. I would just like to thank the gentleman, Mr. Straus, for referring to the small business participating debenture. The ranking Republican member of our Subcommittee on Taxation, as a matter of fact, is rewriting the debenture bill to include an investment tax credit up front of 10 percent, by $20,000. By the way, 3 percent is too low, because the IRS requires at least 9 percent, I believe as of last June, for it to be a legitimate loan. I thought I would pass that on to the gentlemen. I do have a question.

When a bank makes a loan to just any business that walks in off the street without any SBA participation, what is the exposure?

Mr. **Straus**. Exposure to the borrower?

Mr. **Centner**. To the lender, sir.

Mr. **Straus**. Not SBA oriented.

Mr. **Centner**. No. This is a regular business loan, made by a lending institution.

Mr. **Straus**. I do not know what you mean by the word "exposure."

Mr. **Centner**. If the loan is bad, how much do they lose?

Mr. **Straus**. Joe.

Mr. **Acosta**. They just have to pay back the amount of the loan.

Mr. **Centner**. The point I am making is that the exposure of a lender on a loan with no guarantee in it is 100 percent. What is the normal rate that a businessman has to pay in interest to get a business loan from an Arizona bank without any other participation by a Federal agency?

Mr. **Acosta**. Right now, at least 22 percent.

Mr. **Centner**. I think what I am leading up to then is that if you have a loan that is in fact, where the exposure of the lending institution is reduced to 10 percent, why is it then not justifiable to ask that banker to lower his own interest rates? Since the 22¾ percent is not required by the SBA, the lender can lend at anything he wants to. In fact, there are banks who never charge more than 1 percent over prime.

Since you are only at risk for 10 percent of the whole loan in the first place, why is it not justifiable to lower your interest rates to begin with? Why should you get the windfall?

Mr. **Straus**. I wish you would save that question and ask the bankers who will appear on the panel later. If I were a banker I would say because we are running out of capital, and it all depends on that. It is like inventory in a store. If you are starting to run out, you just do not care whether somebody comes in, wants 100 of them at 10-percent discount, because you can sell them all without a discount.

Mr. **Centner**. Again, with the 10-percent exposure, he can sell his 90 percent to the secondary market and make a tremendous amount—35 percent, probably. It just seems to me given those figures that reduction in the loans to half a percent or a point over prime would make a small business guaranteed loan with 90-percent participation by the SBA an extremely attractive financial venture.

Mr. **Acosta**. I agree with you. As the chairman says, the bankers will be able to deal with that.

Mr. **Centner**. I think the bankers say they cannot live with it. But I think if you look at the profit-and-loss statement alone, they can live with that very well.

Thank you, Mr. Chairman.

Mr. **Mitchell**. There is one other factor we need to consider, and that is the amount of money available and who are the safest risks. I have never been any great defender of the banks. However, it would certainly seem to me, given the annualized failure rate of many small businesses, if I have a pot of capital, I would rather give it to a large corporation which has less chance of failure, as in the case of Chrysler, where the Government stepped in to make sure it did not fail, than I would to another economic entity. However, we will hold on that until we hear from the bankers.

Thank you very much.

Our next panel is Mr. Edmund Tang, member, Chinese Chamber of Commerce; Mr. Carl Hamilton, president, Arizona Black Chamber of Commerce; and Mr. Ruben Parra, president, Arizona Mexican American Chamber of Commerce.

If you would all come forward, please.

PANEL CONSISTING OF EDMUND TANG; CARL HAMILTON; AND RUBEN PARRA, ACCOMPANIED BY JOSEPH CASTILLO

Mr. **Mitchell**. Gentlemen, thank you very much for taking the time to participate in this hearing. I would assume that all of you are small business owners yourselves, is that correct?

Mr. **Tang**. Yes, sir.

Mr. **Mitchell**. I really feel very guilty about asking people to come to spend a day with us, a day away from the shop. It can create an awesome number of problems. I am really grateful for your participation.

I called all three names. I see four persons. Would someone introduce the fourth gentleman? Then you can simply proceed.

Mr. **Parra**. I would like to present to you Mr. Joseph Castillo.

Mr. **Mitchell**. Gentlemen, you may proceed.

TESTIMONY OF RUBEN PARRA, PRESIDENT, ARIZONA MEXICAN-AMERICAN CHAMBER OF COMMERCE, ACCOMPANIED BY JOSEPH CASTILLO, BOARD MEMBER

Mr. **Parra**. Mr. Castillo will read our testimony.

Mr. **Castillo**. Good morning, Mr. Chairman, committee members, ladies and gentlemen, my name is Joseph A. Castillo and I am here today to testify this committee as a board member representing the Arizona Mexican-American Chamber of Commerce. On behalf of our constituency we thank you for giving us the opportunity to voice our concerns.

Today there continues to exist major institutional roadblocks and problems which deny our members and other small businesses in

Arizona the opportunity to take their representative and rightful place in this State's business economic mainstream.

Today we will briefly discuss what we consider to be the three major institutional barriers that continue to block the development of Hispanic-owned businesses in Arizona. These are: One, inadequate access to capital resources; two, inadequate access to government and prime contractor-procurement opportunities; and three, lack of comprehensive business development assistance.

We will also make some sound recommendations for alleviating some of these roadblocks. Through the implementation of these recommendations Hispanic and other small businesses will have a genuine opportunity to develop in economic mainstream areas such as the manufacturing, distribution, transportation, communications, finance, and tourism industries in Arizona.

In order for our constituents to have a real opportunity to compete in business, Government must assist us to acquire capital in substantial amounts to enter and develop into growth industries. Historically, we have been declined credit and equity capital for a multitude of reasons, but the main reasons are lack of capital injection by the owner; lack of collateral; lack of track record; lack of managerial experience—experience not well rounded in sales, finance, and production; lack of professional assistance, such as a lawyer, CPA, or professional consultants; and that the applications are based on a traditional service or retail industry, not on growth industry.

These roadblocks have permitted the continued and systematic elimination of Hispanics, other minorities, and small business firms from entering and developing into more productive industries that offer growth and higher profits.

The statistics to substantiate these statements abound, as I am certain your committee is well aware. Let me suffice to say that in talking with area bankers we have been told that approximately 20 percent of business loan applications come from minority business—yet less then 2 percent of these applicants are granted loans.

We believe that in Arizona, the Federal Government needs to provide the necessary leadership to assist us to compete and develop. The majority of our institutional business community and State government continue to refuse to assist us to develop a stronger economic base of Hispanic and other minority-owned businesses and only give lip service.

Unlike other government entities, the city of Phoenix has continued to assist minority and small businesses through small business development assistance programs, such as their community development small business program, efforts to fund a MESBIC and a local development corporation.

Therefore, we, the Arizona Mexican-American Chamber of Commerce make the following recommendations which we deem necessary in order for all small business persons to have a real opportunity to achieve economic parity and thus more social and political stability:

One, decentralize more of SBA's national and regional authority to district offices so that districts may design more financially creative programs within our sphere of influence.

Example: The Phoenix district office tandem loan program. Through this program small businesses in Arizona now have an opportunity to borrow up to $500,000 in long-term debt at lower than current interest rates by combining bank SBA guaranteed loans and SBA direct loans.

Two, defeat current efforts afoot in Congress to water down SBA's lending authority through such despicable efforts as: lowering the SBA bank guarantee rate from 90 percent to 75 percent; limiting the percent interest that a participating bank can charge on an SBA guaranteed loan; increasing qualifying criteria such as credit standards even though most minority-owned businesses don't qualify for credit now.

Three, develop equity capital vehicles in Arizona. Expand the SBA MESBIC and SBIC programs so that we can develop some of these vehicles in the Southwest. Currently, efforts continue to limit or destroy this valuable SBA programs. Pass legislation to provide for corporate tax credits to those financial institutions and corporations that invest capital in minority-owned businesses. Let's give private industry a business incentive (tax credit) for investing in minority-owned businesses. President Reagan should welcome such an opportunity for big business to voluntarily and more profitably help small business firms.

In summary, we need to continue to develop vehicles that will increase our access to debt and equity capital markets—not decrease our access as is being done by current administration action.

The second major problem we face is inadequate access to public and private procurement opportunities. Historically, the institutional barriers between minority business and the Federal Government and Federal Government prime contractor procurements have been so formidable that small business set-asides and the 8(a) program were developed as an effort to assist in penetrating these markets.

As most of us know, these two programs have had some success but are most referred to in terms of abuses and additional redtape, as a result of mismanagement and political agendas. We believe in the intent and concept of these programs and stand ready to speak in their defense if necessary. We further believe that irresponsible bureaucrats should be prosecuted for improprieties and mismanagement of these programs.

In another effort to assist small and minority business, Congress passed Public Law 95-507 back in 1978. Through this legislation it was envisioned that small business would finally take a more participative and representative role in Federal procurement contracts. Most of us today know that while the intent of the law is admirable, the performance required by this law is extremely lacking. When Government agencies themselves do not enforce the subcontracting plan portion of the law—for instance, the Department of Transportation—is it any wonder that prime contractors don't either.

This law is probably one of the most potentially beneficial pieces of legislation for small business, next to the creation of SBA in 1953. Our recommendation with regards to really opening up procurement opportunities to small and disadvantaged business is to grant SBA the authority to take sanctions against those procurement officials and prime contractors that do not implement the intent of the law.

Currently, SBA has the responsibility to monitor contract compliance under section 211 of the law, but no authority to enforce compliance. Unless SBA is granted this authority, this law, like the small business set-asides and the 8(a) program, will work in spurts at best, and be another example of how inexperienced Government managers are at implementing operating policies of this great Nation.

In summary, the Arizona Mexican-American Chamber of Commerce believe that if SBA is given the authority to enforce Public Law 95-507, the small business community will at last begin—and I emphasize begin—to participate in federally funded procurement opportunities in a more representative manner. This single factor will also do more to demonstrate repayability of a debt or equity obligation than any other programmatic or legislative effort and will therefore increase the minority entrepreneur's access to capital markets.

The third major problem facing minority business is lack of managerial and technical experience. Up until July 1, 1981, minority business had access to no-fee management and technical assistance from the Phoenix Business Development Center, a local nonprofit consulting firm. Now the delivery system has been interrupted due to what we perceive as regional and national agency problems. We ask for your assistance in clearing up the apparent mystery why MBDA has not completed their audit and investigative review to determine if the center is to continue to operate their general services program or not.

Our requests to MBDA have gone unanswered. While the center continues its valuable work, minority businesses in Arizona can no longer receive development services by way of the MBDA contract. Your assistance in this matter is vital to many small businesses.

The type of managerial resource at the center has proved, in our opinion, to be an invaluable asset to the small and disadvantaged business community. Increased Federal support to such a program is critical to the continued development of local small business.

For the first time, minority businesses have been able to tie into a corporate and Government-sponsored program of assistance that has resulted in progress for those business persons willing to learn the ways of corporate America. However, this program is grossly underbudgeted and understaffed. From what used to be a $700,800 effort to assist minority business enterprise 4 years ago, it has been gutted to a $262,000 token amount. Our constituents cannot be serviced to any degree of measurable impact with such an underbudgeted program, whether the center regains the MBDA contract or not.

The message of our chamber, Mr. Chairman, is that small and disadvantaged businesses in Arizona continue to need the management and technical services such as those provided by the center. Unfortunately, they are no longer available.

We ask for your involvement to assist us in securing these services again. The business network developed by this organization has taken years to build and now is being threatened, in our estimation, by politically motivated forces.

In closing, Mr. Chairman, we ask that your committee—our standard bearers—challenge the true intent of the current administration's economic policy of reducing inflation; reducing unemployment; and increasing capital investment. We ask this committee to challenge President Reagan's economic policy because many current economic policies are not favorable to small business. In most cases, these policies are negative, as has been highlighted today.

If the President wants to decrease inflation, unemployment and increase the productivity of this Nation, then assistance to small business through such recommendations as those being made today by representatives of the small business community would certainly help this effort.

We need Government support to acquire debt and equity capital. We also need support to secure a representative percentage of Government and Government prime contractor procurement contracts.

In turn, small and minority-owned business will once again begin to grow and put America back to work. It seems to us that simple logic should dictate that our Government should spend more of its resources strengthening the economic backbone of this great Nation.

Mr. Chairman, we ask that you provide our testimony to the President and the Congress for their edification. We must believe that President Reagan, a self-made man, will correct some of the negative efforts afoot within his administration to destroy our advocates, the Small Business Administration and the Minority Business Development Administration. These agencies create and save jobs. These agencies allow for those less affluent the opportunity to succeed or fail in business. These agencies directly increase the tax base of this country by leveraging resources with those of the private sector.

Certainly there are problems within these agencies, but these are problems of mismanagement, not problems with the nature of the agencies. Operate these agencies as envisioned and intended and minority and small business in America will continue to feel that growth for economic and social stability is at a premium, not a deficit.

Mr. Chairman, we hope that this testimony has been of assistance to your committee and we stand ready to support your legislative advocacy efforts.

Thank you very much.

Mr. MITCHELL. Thank you for your testimony.

[Attachments to Mr. Parra's testimony follow:]

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Strategies for Increasing Capital Availability for Small Enterprise in Arizona

-

Interim Report

WORKING PAPERS

15 June 1981

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EXECUTIVE SUMMARY

Arizona's population and business growth has been substantial over the last decade. It has provided jobs and security to many. However, this growth has been largely unchanneled. Those who had the resources could start a business to take advantage of the growth. Business development efforts by the state and local governments were focused on attracting whoever would come, with some focus on electrical equipment manufacturing. And those who did not have the resources were unable to start a business, or to successfully compete. This group tended to comprise local, rural, small, or minority business.

This report is a first cut in examining the role that access to capital has played in the opportunities available to rural, small and minority businesses. It also suggests actions that can be initiated within the state of Arizona to allow for greater participation of these businesses in the growth that has and will continue to characterize Arizona.

Summary of Issues and Solutions

Municipal finance issues will become more important as small towns continue to grow. It will become critical for towns hosting a construction force for any of the variety of new energy-related facilities planned for the next decade. In response we suggest that Arizona consider the following options:

- Encourage project developers to take responsibility for the provision of required infrastructure or to prepay taxes to provide communities adequate up-front resources to develop their infrastructure.
- Establish a community impact account funded by income from mineral leases as an income tax on extraction to serve rapid development areas.
- Provide for regional revenue sharing to distribute the tax benefits of large developments to the towns receiving the impacts.
- Change the bond sale limitations and allow the sale of bonds for infrastructure development.
- Create a municipal bond bank to package small bond issues to national investors.

Long-term commercial-industrial debt is one of the most difficult for small businesses, especially start-ups to acquired. Because of this, several programs have been developed in Arizona to ease availability to small businesses; however, these fall short of need. We propose the following options:

Taxable

- Establish a state-sponsored loan insurance program.
- Help to establish a consortium of commercial banks to pool loan money to make higher-risk loans.
- Improve awareness and information loan officers have for loan decision making considered to be higher risk.
- Increase business development efforts in rural areas.

Tax-Exempt

- Develop an ability to sell umbrella revenue bonds on a state level.
- Target the availability of IRB issues.

Intermediate-Term Debt is primarily for expansion. While it is more available than long-term debt to small business, there is still a definite problem in availability. We propose that:

- An Arizona Business Development Corporation be established to make riskier, targeted loans and improve bank liquidity.
- A set of "leeway regulations" be developed to allow banks to increase risk-taking.

Equity capital is almost non-existent in Arizona for small independent businesses. This must primarily be obtained from friends and family. Strategies in this area include:

- the creation of venture capital organizations, such as SBICs or MESBICs,
- the development of state tax credits or deductions for investment in Arizona businesses.

Capacity building is basic to the needs of small businesses. It is ongoing at the public and private level and can be complemented by the following activites:

- Encouraging Industrial Development Authorities to assess their local needs for jobs and economic development, and to sell bonds for businesses which provide the greatest local benefit and have few alternatives for financing.
- Improve the awareness and information loan officers have for loan decision making on businesses considered to be of high risk.
- Increase business development efforts in rural areas.

Finally, attention should be given to strategies for developing pools of capital from mineral taxation. Taxation on copper production could be improved through combining different forms of taxation to insure that the citizens of Arizona benefit evenly from their mineral wealth.

I. CHARACTERISTICS OF THE ARIZONA ECONOMY

A. State Development Characteristics

Arizona has experiended phenomenal population growth, doubling in size over the last decade. Although the state is not expected to grow as rapidly in the coming decade, Arizona is still expected to be one of the fastest growing states in the country. Official estimates put the growth rate between 1980 and 1990 at 24 percent (Department of Economic Security, 1979). Such growth rates suggest an enormous opportunity for a variety of small business development. Table 1 summarizes growth patterns in Arizona by region and the expected impacts of development on small, local enterprises.

While all planning districts experienced substantial growth between 1970 and 1980, rural districts with significant recreation or retirement development led in this growth. The two major urban counties followed. The parts of the state which showed the least growth were the two rural districts in the southeast.

Table 2 shows some additional information on growth issues. The first three planning districts (the most developed or tourist-oriented) showed the greatest growth in the number of businesses, while the more rural areas showed lesser, although still respectable, rates of growth. In these same three districts the percentage change in number of employees surpassed the growth in the number of businesses, indicating that large employers were attracted. Unemployment rates, quite low in the urbanized districts and uniformly high in the rural ones, also indicate unbalanced development.

Table 1: Growth Patterns in Arizona, by Planning District

Region by County	Regional Center	Regional Population			Important Regional Characteristics	Characteristics of Expected Development or Change	Expected Impacts of Changes on Small, Local Enterprises and Minority-Owned Businesses
		1970	1980	% Change			
District 1 Maricopa	Phoenix	971,200	1,505,400	55.0%	Primary urban center yet major agricultural area. Tourism, service, and manufacturing are important sectors. It is the state banking center. Electrical equipment manufacturing is a growing and important sector.	Increasing urbanization. Growth in all communities. Population, retirement, and light industrial and manufacturing growth viewed as desirable in all communities in the metropolitan region. Possible development of oil and natural gas reserves, an oil refinery and construction of a nuclear power plant.	Growth occurring in all business sectors, with continued need for consumer and tourist services and continued solicitation of manufacturing relocation. With energy developments, concentrated needs will occur for construction goods and services and consumer goods and services (recreation, food, housing, etc.) in more rural areas. Some associated businesses will develop in urban areas.
District 2 Pima	Tuscon	351,700	531,900	51.2%	A major urban area, educational center. Urban and rural tourist attractions. Regional banking center. Proximity to Mexico results in attractiveness to tourists. Many unregistered workers in the workforce.	Manufacturing growth sought, population growth sought and should continue. Electrical service more reliable than in Phoenix, a key attraction to increased electrical equipment manufacturing.	It is expected Pima County will continue its present attractiveness to manufacturing development, growth in consumer goods and services, and tourist services. Without changes businesses will continue to develop as they have in the past.

Table 1 (continued)

Region by County	Regional Center	Regional Population			Important Regional Characteristics	Characteristics of Expected Development or Change	Expected Impacts of Changes on Small, Local Enterprises and Minority-Owned Businesses
		1970	1980	% Change			
District 3 Apache Coconino Navajo Yavapai	Flagstaff, also Winslow, Holbrook, Prescott, Window Rock	165,200	262,700	59.0%	Indian reservations, including a large Navajo Reservation spanning 3 counties, linked by highway. Recreation is a substantial factor as these counties contain the Grand Canyon and numerous other sites. Timber harvesting, coal extraction, and serving tourists are important economic sectors.	Increased recreation, and continued coal extraction likely through 1990. Four projected coal-fired power plants could increase temporary population (in mobile housing) with some addition of permanent operational personnel. These developments are projected to increase electricity production by about 50%. There is also some potential uranium milling in this area, and synfuels processing.	Some growth in tourist service industry expected in the Grand Canyon area. Development of any of proposed power facilities will require rapid growth of construction and consumer goods and services. Existing small businesses will do well except in rapid growth area where they'll have to compete for expensive labor.
District 4 Mohave Yuma	Yuma, Lake Havasco City	86,700	145,200	63.7%	Borders the Colorado River, trade links to California and Los Vegas. River oriented recreation, with discrete centers. Major retirement development area.	Highway bordering the river will further link recreation areas, with likelihood of continued growth. Continued high growth, retirement, and tourist area, with continued development of warehousing function in the Yuma area.	Some manufacturing, wholesaling services will grow in less isolated areas. Residential growth will result in more demand for consumer goods and services. Small businesses could do well as growth is not very rapid, and sectors will expand that are dominated by small businesses

Table (continued)

Region by County	Regional Center	Regional Population			Important Regional Characteristics	Characteristics of Expected Development or Change	Expected Impacts of Changes on Small, Local Enterprises and Minority-Owned Businesses
		1970	1980	% Change			
District 5 Gila Pinal	Globe/Miami	97,800	128,200	31.1%	Major copper mining area, with other deposits minable. Trade and service links with both Pima and Maricopa Counties.	Local uranium and asbestos deposits are not likely to generate any large-scale development. Growth rate to 1990 likely to be less than in the state, as a whole. Future growth dependent on viability of the copper industry and any potential retirement development.	Some population and small mining development will require increased consumer goods and services businesses. Local interest is towards using IRBs for smaller-scale development.
District 6 Cochise Graham Greenlee Santa Cruz	Bisbee/Douglas	102,800	140,700	36%	Transportation and economic connections with Mexico and New Mexico. A tourist area, with closed-down mining activities.	No major energy-related or tourist projects are planned. Population increase projected to 1990 likely to be less than state average. Population growth may occur from influx from Mexico and increased trade with Mexico.	The type of population increase here will lead to attempted increases in large-scale industry or tourist services, some of which may occur. It does not appear to have good new opportunities for small businesses but existing ones are not threatened.

SOURCES: Ronald McMahan and Bennett, Energy Activity in the West, ABT/WEST and WESTPO, March 1981.
Christian Erickson, MX and Energy Development: An Analysis of Their Cumulative Demand for Labor, Materials, and Equipment, ABT/WEST, February 1981.
OEPAD Arizona, A Profile of Economic Resources, January 1981.
Arizona Department of Economic Security, Population Estimates of Arizona, January 1981.

Table 2: Changes in Economic Development Indicators
by Planning District, 1978 to 1979

Planning District Number	% Change in Number of Establishments, 1978 to 1979	% Change in Number of Employees in Week Including 3/12, 1978 to 1979	Unemployment Rate (1979)
1	+8.6%	+14%	4.4%
2	+7.7%	+15%	4.4%
3	+6.5%	+11%	8.7%
4	+5.4%	+ 4%[1]	8.1%
5	+4.7%	+ 1%	7.1%
6	+3.9%	+ 6%[2]	8.3%

[1] Includes only Yuma County as data was not available for Mohave.

[2] Does not include Greenlee County, for which data was not available.

SOURCES: Arizona: A Profile of Economic Resources, January 1981.
Bureau of the Census, County Business Patterns, 1979, Arizona, CBP-79-4.

Overall, growth in Arizona was fueled by manufacturing and business development in the large urban centers (with some in small urban centers), major energy or mining activities, an increase in tourism, and the development of retirement communities in several districts. This same type of growth is still encouraged and will likely continue. The nature of the economic growth in Arizona and the rapidity of that growth have had a variety of impacts on the small business sector in the state. A brief summary of these impacts follow.

Although many small businesses arose in the consumer goods and service sectors, in the tourism industry and in wholesaling to serve local and out-of-state markets, overall, emphasis by the public and private sectors in the state has been placed on large manufacturing concerns that would employ larger numbers of people. Small businesses have thus had to compete with large-scale manufacturing and energy developments for scarce capital and have often lost. With the variety and pace of development occurring and the subsequent large demand for capital, banks found they could be conservative about lending to small businesses with higher risk, perceived lower returns, and high information costs.

Even in the service and retail sectors, small, local businesses are at a disadvantage. Banks have been able to minimize their information costs for loans by lending to franchise outlets which have an advantage over independent businesses because of their market research, management training, and uniform products. As a result, a significant portion of the new service and retail industry in Arizona is likely composed of franchise outlets.

Smaller manufacturing businesses fared better than the retail and service sectors, as manufacturing has always been a popular focus of local development organizations, such as state development offices and chambers of commerce. Resource-based industries have attracted less attention, with small agricultural enterprises virtually disappearing in some areas as competition for water increased.

While rapid localized development, such as some of the planned power facility constructions, will require consumer services and goods, the short-run and cyclical nature of demand suggest these may be bad risks for bank loans. Such developments are more likely to encourage franchise outlets, developer-run stores, or businesses where the owner has sufficient capital on his/her own to develop a business.

Although minority-owned businesses have probably increased in number and viability recently, aided by some of the targeted purchasing programs by local and federal government agencies and through their own organizational efforts, they face unique problems under conditions of rapid development (Arizona Minority Purchasing Council Newsletter, 12/78). With a large demand for capital by businesses with little perceived risk, minority business people may have a more difficult time gaining access to loans. Like other small businesses, they have a need for equity capital that is also not available in adequate quantities for higher risk businesses in Arizona (Mario Corral, 1981). Procurement programs, capacity building and advocacy can help to some extent under present conditions.

Future development holds possibilities for local, small, and minority businesses, but some of the factors currently discouraging their development must receive attention. A deeper look at the different economic sectors in Arizona by region will help define the situation more clearly.

B. Small Business Characteristics

Most of the businesses in Arizona, as in all states, are small businesses by several definitions. While general studies on small businesses often use 20 employees as the cut-off point for small businesses, the Small Business Administration for purposes of making loans, generally defines a business as small if it has less than 500 employees. (In some areas, this can go as high as 1,000 employees [SBA Rules and Regulations, Part 121, August 1, 1980].) Regardless of which definition is used, most businesses in Arizona are small; but, the numerical predominance of small businesses in Arizona does not necessarily imply a healthy small business sector.

Most business establishments in Arizona, as shown in Table 3, are found in the retail trade and service sectors. The number of enterprises in these sectors with less than 20 employees comprise well over half of all the businesses in the state. These are the businesses that are popularly thought of when thinking about small businesses. In addition to these two sectors, the majority of businesses in all other sectors have less than 20 employees.

Only agriculture, forestry, and fisheries have the majority of its employees employed in small businesses. Mining and manufacturing have the major proportion of their employees in businesses with over 500 employees. Other sectors show most employees in businesses with less than 100 employees. Because of the orientation of the state in

Table 3: Number and Size of Establishments by Industry - Arizona[1]

	Number of Establishments	Number of Establishments by Employment Size Class				Number of Employees by Employment Size Class				
		Less than 20	20-99	100-499	500+	Total	Less than 20	20-99	100-499	500+
Agricultural Services Forestry, Fisheries	741	704	35	2	-	4,839	3,173	903	-	-
Agriculture	729	692	35	2	-	4,766	3,100	(D)	-	-
Mining	102	126	30	16	10	21,043	780	1,444	4,412	14,399
Metal mining	64	33	11	11	9	17,255	220	689	2,035	9,416
Contract Construction	5,073	4,426	507	58	2	61,626	24,501	9,833	7,686	D
Special trade	3,250	2,820	398	32	-	37,881	16,107	16,299	5,475	-
Manufacturing	2,562	1,797	585	151	29	121,132	11,844	26,948	31,524	50,816
Electric and electronic equipment	145	82	38	18	7	24,534	566	1,684	1,908 (D)	2,164 (D)
Transportation and Other Public Utilities	1,285	1,001	216	60	8	35,446	5,522	9,383	11,774	8,767
Communication	214	135	52	24	3	10,763	1,076	2,109	3,343 (D)	(D)
Wholesale Trade	3,538	3,010	487	38	3	45,079	17,646	18,093	6,937	2,403
Durable goods	2,298	1,985	290	22	1	7,206	11,618	10,505	(D)	(D)
Retail Trade	13,796	11,936	1,668	184	8	175,226	68,689	68,427	33,027	5,083
Eating and drinking places	3,373	2,582	735	54	2	58,243	17,551	31,094	6,297 (D)	(D)
Finance, Insurance, and Real Estate	4,621	4,150	424	40	7	49,066	17,659	16,203	4,785 (D)	3,293 (D)
Real estate						12,060	6,004	4,464	(D)	(D)
Services	14,423	13,069	1,141	190	23	166,900	59,112	48,457	36,024	23,307
Health services	3,389	3,197	136	41	15	45,384	12,658	6,750	5,367 (D)	5,780 (D)

[1] Excludes government and railroad employees and self-employed persons.

D - information withheld to avoid disclosing figures for individual companies.

SOURCE: County Business Patterns, 1978, Arizona. U.S. Department of Commerce, CBP-78-4.

economic development and risk aversion by financial institutions during periods of rapid development, it is the large manufacturing and mining efforts that have often been the recipients of available capital.

The important and expanding economic sectors in each region, their size, and jobs they provide are of interest. These are shown in Table 4.

Planning District 1 (Maricopa County) shows contract construction to be a regionally important sector in terms of jobs and number of businesses. It also has more than half of the states agricultural enterprises. In terms of employment, resource-based industries are insignificant. This substantial growth in Maricopa County provides numerous investment opportunities for Phoenix-based banks. Additionally, growth that is successful in the county--construction and manufacturing--are the industries best known to the Phoenix financial community.

The picture for Pima County (Planning District 2, including Tuscon) is similar. After retail trade and services, contract construction has more small businesses while manufacturing includes several quite large operations. Mining is a significant sector with several large copper mines, whereas agriculture is a very small sector.

Planning District 3 shows relatively fewer manufacturing firms, although there are several large ones based on processing natural resources (textiles and paper). Coal is a significant mined product with several large mining operations. Contract construction is still important in employment terms, but is by and large a sector of small business.

In District 4, retail businesses are by far the largest employer. Typical of its consumer service nature to its communities of residents--retirees, and tourists--its largest service sector is hotels and

Table 4A: Number and Size of Establishments by Industry - Planning District 1[1]

	Number of Establishments	Number of Establishments by Employment Size Class				Number of Employees for Week Including 3/12
		Less than 20	20-99	100-499	500+	
Agricultural Services, Forestry, Fisheries	469	453	16	-	-	2,533
Agricultural Services	465	449	16	-	-	2,515
Mining	55	47	8	-	-	633
Nonmetalic Minerals except Fuels	23	18	5	-	-	323
Contract Construction	3,015	2,564	405	45	1	41,040
Special Trade	2,014	1,710	276	28	-	26,419
Manufacturing	1,772	1,215	429	108	20	91,543
Electric and Electronic Equipment	114	62	32	14	6	22,532
Transportation and Public Utilities	605	453	109	36	7	22,212
Communication	73	35	21	14	3	6,213
Wholesale Trade	2,335	1,943	354	35	3	33,804
Durable Goods	1,607	1,363	222	21	1	21,116
Retail Trade	7,345	6,227	973	139	6	108,620
Eating and Drinking Places	1,793	1,309	445	37	2	35,860
Finance, Insurance, and Real Estate	2,834	2,499	296	32	7	35,978
Insurance	265	193	55	15	2	7,982
Services	8,787	7,903	740	125	19	110,673
Health	2,179	2,064	83	20	12	29,272

[1] Excludes government and railroad employees and self-employed persons.

SOURCE: Bureau of the Census, County Business Patterns, 1978, Arizona, CBP-78-4.

Table 4B: Number and Size of Establishments by Industry - Planning District 2[1]

	Number of Establishments	Number of Establishments by Employment Size Class				Number of Employees for Week Including 3/12
		Less than 20	20-99	100-499	500+	
Agricultural Services, Forestry, Fisheries	121	116	5	-	-	766
Agricultural Services	119	114	5	-	-	757
Mining	45	30	8	4	3	6,015
Metal	19	9	4	3	3	5,589
Contract Construction	971	822	137	11	1	13,355
Special Trade	620	515	101	4	-	7,706
Manufacturing	353	261	72	15	5	13,536
Printing and Publishing	80	68	9	2	1	1,736
Transportation and Public Utilities	213	151	47	14	1	6,731
Communication	36	15	15	6	-	2,634
Wholesale Trade	557	476	80	1	-	5,908
Durable Goods	394	343	50	1	-	4,032
Retail Trade	2,686	2,296	357	31	2	34,281
Eating and Drinking Places	648	486	151	11	-	11,178
Finance, Insurance and Real Estate	1,014	927	79	8	-	8,473
Real Estate	505	479	24	2	-	2,806
Services	3,018	2,729	242	43	4	35,322
Health	697	651	30	13	3	11,209

[1] Excludes government and railroad employees and self-employed persons

SOURCE: Bureau of the Census, County Business Patterns, 1978, Arizona, CBP-78-4.

Table 4C: Number and Size of Establishments by Industry - Planning District 3[1]

	Number of Establishments	Number of Establishments by Employment Size Class				Number of Employees for Week Including 3/12
		Less than 20	20-99	100-499	500+	
Agricultural Services, Forestry, Fisheries	21	21				B
Mining	14	9	2	3		F, C
Contract Construction	431	415	16			2,472
Special Trade	204	196	8			1,173
Manufacturing	184	149	25	12	1	3,843
Lumber and Wood Products	56	41	10	5		1,924
Transportation and Public Utilities	177	149	22	6		2,543
Communication	28	22	4	2		649
Wholesale Trade	177	168	9			929, C
Durable Goods	100	97	3			595
Retail Trade	1,421	1,281	134	6		12,621
Eating and Drinking Places	359	292	63	5		4,992
Finance, Insurance and Real Estate	274	258	16			1,449
Real Estate	121	116	5			520
Services	1,069	988	71	8		9,097
Health	225	213	8	4		2,303

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[1] Excludes government and railroad employees and self-employed persons.

These letters were entered in place of employment data and represent an employment size class as shown:
B 20-99   C 100-249   F 500-599

SOURCE: Bureau of the Census, County Business Patterns, 1978, Arizona, CBP-78-4.

Table 4D: Number and Size of Establishment by Industry - Planning District 4[1]

	Number of Establishments	Number of Establishments by Employment Class Size				Number of Employees for Week Including 3/12
		Less than 20	20-99	100-499	500+	
Agricultural Services, Forestry, Fisheries	62	47	13	2		B
Agriculture	8	7	1			
Mining	8	6	1	1		E, A
Contract Construction	339	320	17	2		2,684
Special Trade	209	202	7			1,397
Manufacturing	106	76	26	3	1	3,473
Transportation and Public Utilities	100	85	13	2		1,364
Wholesale Trade	172	153	17	2		1,823
Non-durable Goods	86	74	10	2		1,186
Retail Trade	850	765	79	6		7,725
Eating and Drinking Places	220	184	34	2		2,641
Finance, Insurance and Real Estate	204	192	12			1,121
Services	635	590	40	5		4,927
Hotels	84	70	11	3		1,290

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[1] Excludes government and railroad employees and self-employed persons.

These are entered in place of employment data and represent an employment size class as shown
A 0-19 B 20-99 E 250-499

SOURCE: Bureau of the Census, County Business Patterns, 1978, Arizona, CBP-78-4.

largest wholesale sector is nondurable goods. Additionally, several very large agricultural operations are located here.

The east-central district, Planning District 5, shows the copper mining industry to dominate the local economy, with quite large mines. Manufacturing is the second largest sector, with nine large operations and over 4,000 employees. This is quite different from the other Planning Districts.

Finally, the southeastern corner of the state is heavily dominated by retail trade, but with several large mining and manufacturing organizations. It is a very sparsely populated area, with few businesses and an almost non-existent agricultural sector.

The Planning Districts, then, have very different characters, with dominance varying from manufacturing to mining or tourism. One factor is very clear. The state's economy is heavily dominated by Phoenix and Tucson, with their size, growth rates, low unemployment, and manufacturing sector.

Table 4E: Number and Size of Establishment by Industry - Planning District 5[1]

	Number of Establishments	Number of Establishments by Employment Size Class				Number of Employees for Week Including 3/12
		Less than 20	20-99	100-499	500+	
Agricultural Services, Forestry, Fisheries	43	42	1			A, C
Mining	39	20	8	5	6	2,419, I
Metal	22	9	3	5	5	8,406
Contract Construction	126	122	4			799
Special Trade	74	73	1			428, B
Manufacturing	70	41	20	8	1	4,227
Transportation and Public Utilities	74	65	8	1		
Wholesale Trade	102	94	8			784
Retail Trade	666	520	46			1,845, H
Eating and Drinking Places	174	156	18			1,720
Finance, Insurance, and Real Estate	120	114	6			790
Services	403	376	23	4		3,006

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[1] Excludes government and railroad employees and self-employed persons.

These are entered in place of employment data and represent an employment size class as shown:
A 0-19 B 20-99 C 100-249 H 2,500-4,999 I 5,000-9,999

SOURCE: Bureau of the Census, County Business Patterns, 1978, Arizona, CBP-78-4.

Table 4F: Number and Size of Establishment by Industry - Planning District 6[1]

	Number of Establishments	Number of Establishments by Employment Size Class				Number of Employees for Week Including 3/12
		Less than 20	20-99	100-499	500+	
Agricultural Services, Forestry, Fisheries	24	24				B, B, A
Mining	12	7	2	2	1	C, G, A
Contract Construction	189	181	8			1,269, A
Special Trade	95	91	4			483, B
Manufacturing	73	54	13	5	1	2,401, F
Transportation and Public Utilities	115	98	16	1		1,672
Wholesale Trade	192	173	19			1,628
Retail Trade	827	748	78	3		6,920
Eating and Drinking Places	179	156	23			1,848
Finance, Insurance, and Real Estate	173	158	15			1,084
Banking	28	19	9			
Services	510	482	25	3		3,875
Health	89	83	5	1		963

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[1] Excludes government and railroad employees and self-employed persons.

These are entered in place of employment data and represent an employment size class as shown:
A 0-19 B 20-99 C 100-249 F 500-999 G 1,000-2,499

SOURCE: Bureau of the Census, County Business Patterns, 1978, Arizona, CBP-78-4.

II. SMALL BUSINESS DEVELOPMENT AND CAPITAL AVAILABILITY

A. State Economic Development Policy

Arizona business advocates at all levels--from local chambers of commerce to the Governor's office--expect that economic growth in Arizona will proceed at a slower pace than that experienced in the previous decade. As a result, sectoral and geographic business needs are becoming more apparent, with the state government now having the luxury of targeting its policies toward specific goals. Interviews with a broad segment of the development community in Arizona (see Appendix for a list of interviewees) identified the following general economic needs:

- the continued creation of additional jobs for Arizona residents,
- diversification of industries, broadening the economic base,
- rural economic development to equalize growth in all parts of the state,
- development targeted to specific needs, including minorities, low-income communities, and central city redevelopment.

Although the unemployment rate in the metropolitan areas is low, the constant influx of new residents, relatively high unemployment in rural areas, and the cyclical nature of tourism, mining, and agricultural employment has prompted state officials and the business community to constantly seek the establishment of new businesses. The primary focus of these job-creation efforts has been the attraction and relocation of established firms from other states. The Tuscon Economic Development Center, the state Office of Economic Planning and Development, and others have established extensive marketing programs that promote the Arizona business climate, and regularly take recruiting trips throughout the nation. The chief emphasis has been the attraction of manufacturing firms. To complement these efforts, both public and private sector job training programs provide skills to Arizona residents to fill these newly available jobs.

Past success has prompted a continued marketing effort. Manufacturing employment in Arizona grew at four times the national rate over the past decade. In just the last year, January manufacturing payroll dollars were 13 percent higher than in January of the previous year (Phoenix Business Journal, 5/11/81). Interestingly, a national survey assessing attractiveness of states for business location showed Arizona's labor attributes (low union activity, low net worth of unemployment compensation trust fund, and low unemployment benefits paid) to be more persuasive than any other factor (Phoenix Business Journal, 5/11/81).

Efforts at economic diversification have followed a largely similar pattern, based on the interstate relocation of existing establishments. The major targets here have been electronics and data processing firms, to complement the predominance of other manufacturing and construction in the urban areas. Diversification in rural areas has been sought to stabilize a cyclical agricultural or mineral base. Such developments vary, but examples include an out-of-state transportation company locating a facility in Winslow, or an effort to attract other mining and recreation activities to the Globe-Miami area.

Diversification in local areas is closely linked with rural development of any kind--both recognize the need for large and more stable economic sectors in many of the state's rural areas. With the rapid growth of the last few years, Arizona has found itself one of the most urbanized states in the country, with 85 percent of its population living in urban areas. Rural areas have been growing, but generally without the sound economic structure they need. The state has shown its concern for these issues through mechanisms such as the Governors Conference on Small Community and Rural Development held in September of 1980. Discussions at this conference resulted in calls for activities such as:

- establishing local business development groups and attracting more state business development efforts to rural areas,
- increasing the quality and quantity of rural housing through the development of a housing authority or the use of industrial revenue bonds for low-cost housing finance,
- attracting more private financing for housing and business and investigating where presently available financing goes,
- encouraging financial institutions to work with local communities to develop financial resources for rural economic development--including training programs for bank personnel,
- implement a state loan guarantee program,
- examine the impact of state spending limitations on the ability of local governments to support economic development.

These needs, identified by a broad spectrum of rural residents and planners, are supportive of the state's present rural development initiatives, yet point important new directions the state can take. Already, a new office is being established in the Governor's office designed to advocate the needs of rural businesses.

Targeted development, especially minority group business issues, have come more into the forefront. Arizona Minority Purchasing Council is one effort to turn the focus of governmental agencies towards purchasing from minority-owned businesses. The City of Phoenix has been particularly successful in such efforts.

Government programs specifically focused on small business and capital availability are few. The work of OEPAD is the most direct effort in serving business. OEPAD provides needed information for businesses, assists in loan packaging for manufacturing firms, and jointly sponsors workshops and activities in business issues and management with private organizations.

Arizona prides itself as a state open to business growth and development, its primary marketing tool emphasizing a favorable tax and regulatory environment. While business in general is favored, there is little targeting embodied in state law favoring local, small, or rural business development.

Constitutional provisions affecting the business and capital environment include:

- prohibition against the state lending money for private benefit,
- state spending limited to 7 percent of total personal income,
- property tax levy limits for counties, cities, towns, and community colleges.

Legislation affecting the business and the capital environment include:

- presence of a right-to-work law attractive to businesses,
- use of state tax deduction on federal and state income tax resulting in a low corporate income tax rate
- exemption from Arizona corporate tax of income paid to a parent company by a subsidiary
- businesses are allowed a tax loss privilege, permitting the carrying forward of net operating or capital losses,
- sales tax exemption on the sale of machinery or equipment used directly in manufacturing, etc., and solar energy devices,

- no long-term debt or obligation bonds in excess of $350,000,
- spending limits for counties, cities, towns, community colleges and school districts,
- rates of unemployment benefits,
- one-stop permitting for business licenses.

The composite of these laws, including low taxes, are conducive o business growth and relocation. The companions of low taxes are the .aws requiring states to limit spending, tending to preclude direct state financing--by bonds or otherwise--of housing or small business development. Further, it limits the state's imagination in the creation of additional programs since any new initiatives would have to be predominantely self-sufficient.

Two sources cataloguing a variety of state legislation and programs, addressing both the needs of small business and minority businesses, show Arizona to have no legislatively mandated programs in either (Minority Contracting Reports, 3/80 and U.S.S.B.A., 7/80). It is noted, however, Arizona has informal programs for assisting small businesses (OEPAD), for procurement, and for complaint handling.

B. Private Finance Institutions - Policies and Practices

1. Commercial Banks

Arizona, a state which allows branch banking, has three banks with a large number of branches--First Interstate Bancorp (150), Valley National Bank of Arizona (202), and the Arizona Bank (91)--and several banks with between 10 and 30 offices. A majority of state-chartered banks are independent, single-office banks. Of those, only two are located in rural counties.

The heavy urban concentration of Arizona's population has left many rural communities with access to none or only one bank. Even in cases where more than one bank is present, there is little competition between banks for financing opportunities. Litvak and Daniels (1979) identify how the lack of banking competition leads to risk-aversion on the part of commercial lending, a pattern that channels available funds away from higher-risk small businesses.

Most of the total bank assets ($13.4 billion) are held by nationally chartered banks. Overall, the net loans as a percent of deposits in Arizona differs depending on the size of the bank. The larger state banks tend to have loan-to-deposit ratios in the high seventieth percentile while smaller or rural banks had percentages only in the high sixties. This suggests a lending approach that is more conservative in rural areas that are in most need of business development. Interviews with the business community support the perception of Arizona commercial banks as being somewhat conservative in their lending policy. This is further expressed by their mean debt-to-net worth measure (3:1), high collateral requirement, and shorter-term loans (Phoenix Business Development Corporation, 1981).

It was particularly noted that literally no long-term loans were available for small business without an SBA guarantee. The opinion of rural residents was that rural bank branches were even more risk averse, accepting only the least risky loans in rural areas and exporting remaining capital to urban areas. There was a definite feeling expressed in these interviews and echoed in the Conference Report, Governors Conference on Small Community and Rural Development (OEPAD, 1980), that capital was not available for higher-risk, local, small business development.

State banking regulations governing the chartering and branching of banks are significant elements affecting the investment picture in a state. They will be examined in greater depth in the final state report for this project.

2. Savings and Loan Associations

Most of Arizona's 225 Savings and Loans Associations are state-chartered and regulated. Overall, they have 74 percent of their total assets in mortgage loans and 8 percent in other loans, including consumer loans.

Under the HR4986, the Bank Act of 1980, savings and loans associations in Arizona, with both federal and state charters, can now lend up to 20% of their assets for commercial and industrial long-term fixed-asset financing. This is equivalent to $1.3 billion in Arizona. This opens up a substantial new source of debt capital for business that can be of value in business loans to both the Arizona economy and the faltering savings and loans industry.

With the presently high interest rates and substantial inflation in the housing markets, the financing that savings and loans can provide has not been adequate to assure housing for Arizona residents. Additionally, increased use of S&L assets for business loans could further aggravate this situation.

C. (Due to the apparent small venture capital community in Arizona and the absence of interviews with the financial community, we will present information on the venture capital community for the final report.)

III. PROPOSED MODELS FOR SMALL BUSINESS FINANCE: A STATE AGENDA

Businesses and communities need quite different forms of capital in order to develop, start up, or operate programs or operations. A brief introduction to the types of capital that are required will form a backdrop to the discussion of capital availability in Arizona.

- Municipal finance - needed by local and state governments to provide infrastructure such as schools, roads, and waste disposal, to complement and encourage economic growth. Since localities generally obtain capital through the sale of public bonds, they become competitors alongside all other capital demanders in the private marketplace.
- Long-term debt capital - needed by private businesses for start-ups or expansions, and is used for the purchase of land, construction of plant machinery or equipment. Long-term debt comes in two basic forms, taxable (regular long-term business loans) or tax-exempt (usually in the form of publicly issued industrial revenue bonds).
- Long-term housing finance, also available as taxable and tax-exempt investments. Savings and loans have been the traditional providers of residential mortgage lending. State housing finance authority bonds are recent sources of finance for qualifying low- and moderate-income purchasers.
- Intermediate-term debt - generally obtained from commercial banks, this comprises loans of from one to seven years in length and is used for asset expansion and general business cash flow.
- Equity capital - money that represents part ownership in an operation. It is critical in leveraging debt capital, as equity reduces the risk that would otherwise have to be absorbed by debt lenders. It can conventionally be obtained from the sale of stock, from a venture capitalist, or from personal loan sources.

With these in mind, specific capital needs in Arizona will be described along with suggested state roles that can help fill these needs.

A. Municipal Finance

Communities require funds for infrastructure installation and operation. Infrastructure is usually financed through the sale of bonds that are paid off from tax revenues coming in from service users. Infrastructure development is critical to this study in several ways. First, it creates services (i.e., sewer service and streets) necessary to the operation of many business enterprises. As its name implies, public infrastructure is uniquely the responsibility of the public sector, thus public policies in the timing and placement of services greatly affects differential geographic growth rates.

Municipal finance becomes a critical issue in rural towns anticipating rapid large-scale development. Rapid development towns include those with increased coal mining and coal-fired power plant construction in Planning District 3, oil and gas developments (including a possible refinery) and a proposed nuclear power facility in Planning District 1, and planned growth in tourist, recreation, and retirement facilities in several districts.

Concentrated development implies large population influxes and creates a need for local services before the tax base grows to provide service finance. For example, sewers must be built to support the construction of housing for an expanding labor force, but property taxes and user fees required to pay for the sewer may not be available for several years.

Rural governments have very small internal resources, are relatively unknown to public bond buyers, and generally cannot put together the size of bond issue that would be readily acceptable to a public placement. Further, FmHA cutbacks have reduced the availability of the other major source of debt finance.

In addition to finance problems inherent in these situations, several provisions of Arizona law create special hardships for municipal finance. General obligation bonds have a maximum size of only $350,000. Similarly, there is a constitutional debt limit for counties, cities, and towns and a recently passed limitation on increases in the taxable value of locally appraised property. While the direct impact of these laws is not know, such laws can impede the ability of a town to react in periods of rapid growth.

Recommended options for Arizona in the area of municipal finance include:

- Encouraging developers to take an increased role in the provision of required infrastructure.

Planned unit developments, site plan review, and negotiated preservation of public space are growth control mechanisms used successfully in other states. Development costs would usually be capitalized in the sale of homes or lots to the consumer. Second, the state could consider giving a developer the option of prepaying the present value of future property taxes that would act as a credit against future levies. Again, any cost to a developer could be capitalized on sale of property to the ultimate purchasers. Giving developers an option makes the prepayment more flexible and avoids legal issues of unfair taxation.

Such provisions can be directly negotiated between impacted communities and developers, mediated by regional or state agencies. The tenor of such negotiations is dependent on issues such as the size of the development, the amount and siting of new housing, and the amount, cost, and siting of infrastructure developments. Alternatively, enabling legislation may be necessary to ensure participation. Occasionally, towns have negotiated the delivery of prepaid property taxes by the facility or housing developer to allow communities to develop their own infrastructure development. In such situations, the prepaid taxes would be credited against future taxes.

- Establishing a community impact account, funded by income from mineral leases or an income tax on extraction, to serve rapid development areas.

This proposal, similar to a Montana program, would derive revenues by increasing the lease income from mining operations taking place on state land, or establishing a severance tax on non-renewable resource extraction. Funds would be held in a special account and disbursed by a state impact board in the form of direct grants or loan money to communities impacted by large-scale development.

The legislation in Montana places income from a severance tax on coal in a permanent fund to be used to mitigate local impacts, to fund education, and to fund highway improvement in coal mining regions. The local impact money goes to counties, and can be used for land planning, parks acquisition, renewable resource development, and alternative energy research. Money is awarded to impacted communities based on need, degree of severity of impact from the coal development, availability of funds, and degree of local effort in meeting these needs.

A discussion on the type of tax and minerals for which it could be used is included in section IV, "Mineral Taxation in the Four Corners: Some Initial Thoughts."

- Providing for regional revenue sharing to enable communities with large service demands to share in revenue gains originating in increased tax base of surrounding jurisdictions.

In many boom communities, counties experiance heavy service demand even though population growth occurs inside of municipal boundaries--and outside the taxing power of the county. Tax proceeds from major developments in an area could be spread through the entire impact area if revenue sharing were adopted. In such cases, a formula would have to be developed to guide the equitable distribution of funds.

- Changing the bond size limitations and allow the sale of bonds for infrastructure development.

With the present ceiling on bond sales in Arizona, only the smallest infrastructure needs can be met if these limits apply to towns. This is the only solution relevant to towns with simple population growth situations as opposed to large facility development.

- Creating a municipal bond bank to package several small issues together into a larger pool that would attract national investors.

The traditional source of funds for large issues by municipalities and bond banks is the public market. For example, the Vermont and Maine municipal bond banks use Goldman, Saghs as underwriter, aiming to sell to wealthy individuals, commercial banks, and casualty insurance companies. Small issues--single counties or local units of government--would otherwise fail to capture the attention of these investors, having local banks as sole placement possibilities.

State pooling mechanisms used elsewhere have used secondary backups to insure against bond defaults and thereby make bonds more salable. After exhausting the tax resources of the defaulting community, the bond bank could turn to bond credit insurance, the bank's built-up reserve fund, then the state's moral obligation as security.

An Arizona bond bank could operate statewide or, alternatively, it could be a regional bond bank that serves rapidly developing rural areas. In Utah there is a sub-state bond bank, CURIC (Central Utah Rural Impact Capital Corp.), operating in the six counties where the Intermountain

Power Project is being built. CURIC is particularly innovative because it has been organized as a non-profit corporation, without the need for state-enabling legislation. Its only drawbacks are that it cannot provide the entire range of reserve backup available from a statewide bond agency, and it serves a small area, and thus has a limited range of bonds it can package together into the larger issue.

Another possibility to explore, however, is some type of a direct linkage between bond issuers and a mutual fund such as the one Fidelity Group recently established to invest in municipal bonds. It buys up to 5% of any single issue, meaning that the smallest practical bond size would have to be $20 to $25 million. Probably only a state or interstate bond bank could provide issues of this size.

One institutional design issue is whether the municipal bond bank needs to be a separate institution, as it is in Vermont, Maine and Alaska. Utah, for instance, is considering formation of an agency that combines a bond bank and an industrial revenue bond authority into one entity.

B. Long-Term Commercial Industrial Debt

1. Taxable: Long-term debt from commercial banks has largely been focused towards larger businesses and manufacturers, well-established and in need of capital for expansion. Most larger firms can borrow on the basis of established credit, while small businesses seeking to expand have only market potential and built-up assets to act as debt security. Several programs are presently operating in Arizona to alter this limitation and direct long-term loan resources to a wider variety of businesses. These will be briefly described here to establish the level of need for further efforts.

The Small Business Administration (SBA) has the largest finance effort directed towards small businesses, providing both direct loans and loan guarantees. In Arizona, about 58 percent of all SBA transactions are with minorities, 30 percent with women, and 26 percent for manufacturing businesses. The bulk is in retail and service loans. Senior Corps of Retired Executives (SCORE) is a popular program, with 5,000 to 7,000 business participants a year seeking management expertise. They also help federal government purchasing departments use set-asides for minority contractors by signing federal contracts and obtaining a subcontractor themselves (Moreland and Trimboli, 1981).

The SBA employees in Phoenix did not seem optimistic about their future role. Budget cutbacks have reduced SBA funding by about 25%, and the level of federal loan guarantees has been reduced from a maximum of 90 percent to 70 percent. Present opinion is that SBA loan officers must make fewer higher-risk loans and to guarantee only the minimum absolutely required by the bank. By doing this, the SBA program will not have to change drastically. They will have to become, however, more risk averse.

Reaction from others in the economic development community was that the SBA programs do not meet the needs for guaranteeing riskier loans, whether they are located in a rural area, are an innovative enterprise, or are a start-up. Very little money, if any, is available for start-ups. Additionally, the interest rates above the prime make the cost of capital prohibitive.

The Farmers Home Administration (FmHA), Business and Industrial loan section, loans for business and infrastructure development in rural areas. The FmHA loans at prime plus a point. The expense of annual financial statement requirement precludes very small businesses from working through them. With the poor interest terms and risk-averse nature (no research and development loans, most for expansions), there are still many needs not being filled.

Finally, the Tucson Local Development Corporation is a member of a class of corporations authorized under Arizona law to facilitate the financing of land and buildings. They also use the SBA 503 program to sell government-backed bonds to create a pool to provide business loans. Their major goals are job creation and economic diversification. TLDC follows SBA eligibility guidelines but charges high interest and takes only as much risk as SBA programs allow.

The TLDC is the only local program, other than the two federal programs (FmHA and SBA), actually directly loaning money. On the other hand, many of their decisions are based on the federal SBA guidelines. The other organizations can only assist businesses in improving procedures so they are more eligible for loans or try to influence the banks decisions. Only the PBDC expresses active interest in creating new loan programs targeted toward a broader, riskier business audience.

There are a variety of solutions that could increase the availability of long-term debt finance opportunities for small, local and minority businesses.

- Establish a state-sponsored loan insurance program.

Under such a program, the state would target particular types of development that it felt were especially beneficial to the state's economy that could not get money elsewhere due to the riskiness of the business. The state would administer a loan insurance program that would receive its operating expenses and insurance resources from insurance fees paid by borrowing firms. In this way, businesses that can afford the insurance can have access to loans from banks that might not otherwise be available.

A California loan credit guarantee program shares the cost of insurance premiums equally between the borrower, the lender, and the state. The program is automatic in its execution, with the state share kicking in automatically according to whatever terms are agreed upon by the borrower and lender. Thus, the program needs state appropriation, but little bureaucratic administration.

- According to new federal guidelines, federally chartered savings and loans have been allowed to put up to 20% of their deposits into long-term commercial debt instruments. A similar provision amending the state's "legal list" would open up a whole new source of business finance funds.

- A key additional action would be the creation of secondary markets outside of Arizona to import capital, which can be made available in relatively small units for industrial, commercial, and housing purposes. Empire Savings & Loan in Denver (the fourth largest state savings bank) packages commercial mortgages made by other S&Ls for sale to long-term portfolios such as public employee retirement systems.

Short of some type of insurance, taxable long-term mortgages can be resold only where the market itself chooses to invest. The more secure the investments, the more activity there will be in the secondary markets, thereby generating liquidity for originators. Like Colorado, North Carolina has recently begun a program where the public employee pension funds buy home mortgage-backed bonds from S&Ls. The banks and S&Ls sell mortgages to a new corporation which buys private insurance and packages them into pass-through bonds for investors.

2. Tax-exempt commercial debt (Industrial Revenue Bonds): Tax-exempt long-term debt provides an excellent way the state can target its economic development. IRBs are state enabled, and the list of eligible projects can be tailored to meet sectoral needs. One advantage of this type of tax-exempt financing is that often project decisions on making bond sales available to a developing business are made locally by a board that knows the area and its needs, it is lower-interest money for the recipient, and the bonds can be sold on a national market.

Industrial Revenue Bonds (IRBs) are sold on a county and municipal level in Arizona by local Industrial Development Authorities. Bonds generally have a two to three percent lower interest rate, permit 100 percent financing, and can be used for a wide variety of facilities. They can be sold in a $1 million limit or $10 million limit package.

While IRBs have been used successfully in a variety of cases, there have been some complaints that they have been used for businesses that could have found financing elsewhere, and they have not been used for local small businesses but for large, out-of-state owned enterprises. This was particularly noted in Gila County where the large mining companies have been the only recipients of local IRBs.

Improvements have been suggested for the future sale of IRBs in Arizona.

- Develop an ability to sell umbrella revenue bonds on a state level.

Often small businesses have expansion needs too small to justify a separate bond issue. And, sometimes, rural counties do not have sufficient demand to make up a county-wide umbrella bond sale. It would be useful to have a state level development authority, similar to one in Connecticut, capable of selling umbrella bonds that can package a number of small business finance needs together. A state-sponsored credit insurance program to back up this entire package would make the bonds more salable.

The purchasers of tax-exempt bonds are primarily taxable individuals and institutions (commercial banks and casualty insurers). The demand, however, is not unlimited. Individuals and commercial banks have many other attractive tax shelters to invest in, and casualty companies are faced with very uncertain revenue and income streams.

One possibility is to put together pools of IRBs and arrange private placements with the casualty insurers. Connecticut is currently working on this, and there is no reason why Colorado could not do the same. A second idea is making a private placement with tax-exempt, IRB mutual funds, which have been developed by the Fidelity Group, Merrill Lynch, and others.

Fidelity has a new unit investment trust which invests in variable rate IRBs. Fidelity buys the IRBs from banks, which continue to service the bonds and must retain a portion. The bonds have to be rated A or better and in issues of $1 million to $5 million. Also, the banks must agree to take the bonds back--a "put-back"--if lots of investors redeem their shares at once. Fidelity is currently working on developing placement relationships with New York, Minnesota, California, Boston, and Chicago banks.

- Target the availability of IRB issues.

Unlike states like Massachusetts and Connecticut, Arizona municipalities face few constraints on the types, sizes, and locations of firms using industrial revenue bonds. For example, Massachusetts designates commercial area revitalization districts (CARDs) in which there are strong constraints on how IRBs can be used to support retail and service development, and also on the extent to which they can refinance a firm's capital rather than purchase new capital. Designing appropriate constraints, for example, would give Arizona the ability to encourage the types of retail and service sector development it wants. Moreover, bonds could be targeted to specific geographic areas requiring business development--rural counties or low-income urban neighborhoods are possibilities. Minority-owned firms located anywhere in the state could be an exception to the IRB spatial target.

C. Intermediate-Term Debt

Intermediate-term debt, for expansion and equipment, is often hard to come by for small businesses seeking expansion. While intermediate-term debt is available from banks, and some of the other programs operating in Arizona to provide long-term debt (SBA programs, etc.), there is presently no special mechanism to target intermediate-term debt to businesses in need, ineligible for other sources, and with an eye toward economic development. The availability of intermediate-term debt could be increased by creating an effective Business Development Corporation or by developing leeway regulations.

- Establishing a Business Development Corporation.

A chief mechanism used in many states to provide intermediate-term debt is called a business development corporation (BDC), often also termed a development credit corporation (DCC). It appears that Arizona has no enabling legislation for BDCs at present.

BDCs can be chartered through state-enabling legislation that establishes incorporation criteria and requirements. BDCs are privately owned, generally capitalized by industrial and private investors and state banks, and usually operate on a statewide basis. They obtain initial capital from the sale of stock to businesses, banks, and local development organizations. Commercial banks comprise the largest number of participants. A major limiting factor is that stocks yield low dividends, so investors must largely be motivated to invest by prospects of social benefits or indirect profit. Successful BDC investments can help a region's economy prosper, a vitality linked with the long-term survival of area banks.

BDCs exist in 27 states, but just five of the institutions accounted for one-half of total loans. They were more popular in the 50s and 60s and have not been heavily used recently. Several shortcomings help to account for this: Many BDCs have risk-averse staffs and often lose good loans to their member banks.

In addition to using their basic capital to make short and intermediate loans, some BDCs own SBICs so they can also provide equity capital. Another major role they can play is to act as intermediaries, buying SBA-guaranteed loans from banks, packaging and reselling them to organizations such as a public employee pension fund. In this way, pension funds can safely invest in local businesses, and more of the bank's money is available for other lending. A BDC could follow the model of the Kansas Development Credit Corporation and undertake the sec[illegible]ry marketing of SBA loans. In other cases, banks are beginning to develop direct links to pension funds.

Most BDCs lend to small in-state manufacturers which are not eligible for conventional loans. A BDC can make an entire loan or participate with a conventional lender, often in a subordinated position. Occasionally, they accept unconventional collateral.

- Develop "leeway regulations" to allow banks to make more risky loans.

Bank regulators examine loss rates and not portfolio yield, a type of examination that practically prohibits banks from making risky (but high-yield) loans. Leeway amendments would allow a bank to set aside 3% to 5% of its assets for these high-risk loans. This high-risk portfolio would be separately evaluated by bank examiners who would consider its overall yield expectations rather than for each separate loan. In this way, the economic development benefits of riskier small business loans could be realized without violating banking regulations.

D. Equity Capital

Equity capital is not readily available in Arizona and appears to exist only from a few sources. There are a few venture capitalists in the Phoenix and Tuscon areas, who tend to invest in limited cricles. While they make a positive contribution, the small businessperson remains subject to seeking equity from second home mortgages, friends and other family members.

Franchises often provide equity (with a set percentage return) to their franchisees. In fact, it appears that both SBA and banks tend to more readily approve loans to franchisees than to independent small businesses. It seems common, however, that franchisors actually have a controlling interest in the business. These have been important sources of equity to small business people in a state like Arizona with little equity and recent rapid growth. This is primarily true in the retail and service areas. Franchisees are often largely controlled by large corporations and have better access to both equity and debt than small, independent businesses.

Equity, then, is difficult to obtain for those out of big finance circles and whose friends and neighbors have little money to invest. In Arizona, this includes small or minority businesspeople desiring control in management procedures.

Arizona has a number of options, short of direct state involvement, for increasing the amount of equity available to these businesspeople.

- Credit venture capital organizations in Arizona, such as SBICs or MESBICs.

There is an effort underway now, spearheaded by the Phoenix Business Development Corporation, to create Arizona Venture Capital, Inc. Proposed to be an affiliate of the PBDC, it already has $600,000 pledged to it from industry and the city of Phoenix.

SBICs are privately owned and operated investment companies authorized by the federal Small Business Investment Act of 1958 and licensed by SBA. Their purpose is to provide equity capital and long-term loans to small firms. They can also provide management assistance. In addition to investments from local industry, they can also obtain a government-guaranteed loan equal to three times its paid-in capital and surplus. Interest rates on loans are one point below conventional lenders and never higher than 15 percent. In making an equity investment, an SBIC is not allowed to take a controlling interest unless it develops a plan to relinquish control. Different from other equity capital, SBICs can invest in a wide variety of businesses, including construction, retail and wholesale.

MESBICs were allowed by 1969 legislation, focusing on businesses owned by socially or economically disadvantaged persons. They function similarly to an SBIC with several advantages.

There is presently a 90-day freeze on the federal level on licensing SBICs. It is expected that when the freeze is over (on July 17, 1981) that SBIC applications can once again be accepted and processed. The MESBICs program receives its funding by annual congressional appropriation. It is expected that these direct appropriations will be discontinued. It was suggested that an effort could be made to secure some MESBIC funding from the overall SBA budget (Pat Wilkinson, 1981).

- Develop state tax credits or deductions for investment in Arizona businesses.

Arizona is highly dependent on out-of-state headquartered firms investing their money outside Arizona. Providing them, a firm, or an individual a tax credit for in-state investment in venture capital would bring more money in-state of a sort that is sorely needed. This, of course, should be tied to investment in a well-managed and licensed venture capital organization. Another option is for the state to exempt from taxation capital gains of businesses that are invested in Arizona firms, if they were reinvested in other Arizona start-ups.

IV. OTHER STATE AGENDA ISSUES

The previous section of this report reviewed state options in the area of finance to facilitate the flow of capital to small, rural and minority businesses as well as rapidly growing areas. This section looks at two policy areas, not directly involving existing or new financial institutions, which could increase capital availability for small enterprises and development-impacted communities in Arizona. These two policy areas are: capacity building directed at target communities, individual business people, financial institutions, the business community and government; and mineral taxation to increase the flow of revenue to the state and allow for the creation of a "trust fund" which could be used as a source of capital.

A. Capacity Building

Often lack of access to capital by small businesses is not caused by a capital shortage or by imperfections in the capital market. Rather, it results from the lack of management capacity on the part of the community, businessperson or the financial institution.

Capacity building is a mechanism which can be used to target available capital to sectors that may not have ready access because of a lack of skills or information. The term can refer to building capacities of a number of participants in the lending process:

- Targeted communities - communities in need (rural, minority, low income, etc) can learn to identify and assess their development needs and how to develop projects to meet those needs.

- Individual businesspeople - those wanting to start businesses can learn to assess what might suceed in their communities, how to secure financing, how to package a loan, and necessary management expertise.
- Finance institution loan officers - they can learn to examine more closely the communities they are lending in, what the real risks and returns are, and how to facilitate the lending procedure.
- The business community - the business community has organized itself into several advocacy organizations for business issues. They can learn what the issues are for businesses who do not presently have access to capital and help advocate for their needs.
- Government - government can play a large role by setting a business tone favorable to local, small business development and establishing the types of meetings and research required to make the necessary advances.

Presently in Arizona there are a number of exciting organizations that are involved in building capacity. Some of these institutions are described below.

The Phoenix Business Development Corporation (PBDC) performs a variety of services for small businesses in the Phoenix area. They offer no-fee loan packaging to small businesses, provide management technical assistance, and do general advocacy and organizing in an effort to improve the capital availability climate for small businesses. PBDC obtains most of its operating money from government contracts, grants, and fees for service. They feel they have been quite successful in generating businesses and jobs that return to city coffers more than they take out. For example, they estimate that for every $4 Phoenix puts in PBDC, they have developed $17 in taxable income.

Their major effort, then, has been in helping old and new businesses with loan and management assistance with the goal of expanding jobs and the tax base. Their effectiveness has demonstrated the need for other such efforts.

The Arizona Community Action Association, a consortium of non-profit organizations, helps small businesses, primarily in rural areas, obtain long-term financing through loan packaging and management assistance. Their major focus is on creating jobs and growth in rural areas.

While they have several successes, it is basically a small program that can only assist targeted businesses in obtaining bank or SBA loans.

The Arizona Office of Economic Planning and Development (OEPAD) in part plays a similar role to PBDC. OEPAD acts as a liaison between businesses and government to assist in expansion, tax issues, etc. Their primary work is with manufacturing firms. They do some work in assisting in the packaging of loans. It appears that the major effort here is in attracting manufacturing expansions and relocations from out-of-state and assisting in their relocation.

There are a number of other organizations, such as Chicanos Por la Causa and the Chamber of Commerce that are advocacy organizations which promote small business development, but those described here more directly intervene in the process of building the capacity of business and finance people to directly improve access to capital.

These groups comprise a strong network of not-for-profit organizations representing a wide variety of special interests--minority businesses, low-income community development, economic growth and small business development. Members of the network are familiar with and respectful of each other's work. Some members have already collaborated in sponsoring conferences and workshop sessions. They provide a strong base for healthy local small business development in Arizona.

In a present effort to build the capacity of loan officers, the SBA is using Arizona as an experimental state in which they are educating in-house bank loan officers to directly process SBA loans to streamline the process. In an effort to increase interest in rural business and add another organization to advocate for business needs, a rural business development office is in the process of being established in the Governor's Office. This office would target capacity building directly to rural businesses. Other possible state options in the area of capacity building include:

- Encouraging Industrial Development Authorities to assess their local needs for jobs and economic development, and to sell bonds for businesses which provide the greatest local benefit and which have few alternatives for financing.

In many cases the small, locally owned business is more effective in these respects than are the larger, externally owned operations. Coordination and education programs on a state level seem advisable.

- Improve the awareness and information loan officers have for loan decision making on businesses considered to be higher risks.

It has been suggested that the state or a private business management organization run training programs for bank loan officers to make them aware of sectors which have special difficulty in obtaining loans. By learning more about the sectors and the risks they are really subject to, it is felt the loan officers could make better, more equitable decisions.

- Increase business development efforts in rural areas.

A first step has been taken here in the establishment of a rural business office in the governor's office. Rural business development efforts can be undertaken by communities, by chambers of commerce, and by the establishment of other non-profits outside the urban centers. A small version of PBDC in Flagstaff or Yuma might be helpful in assisting local business people in securing both debt and equity capital.

B. Mineral Taxation in Four Corners: Some Initial Thoughts

Early sections of this report reviewed the relative size of existing capital pools in the private market, showing that business capital demand, housing finance, and municipal infrastructure demand all outstrip the abilities of local financial intermediaries to provide capital. Accordingly, models presented in the previous section tried to show alternative ways of plugging into the national secondary markets to import sufficient funds to meet demand. There is a great deal of chance involved in triggering the desired response. Arizona must assume the private market is willing to invest in state projects on the terms beneficial to the state.

There does exist an enormous amount of potential wealth in the state of Arizona that is capable of providing a capital base for the growth of the economy--the rich deposits of natural resources. This section of the draft report presents some basic data regarding the relative size of resource wealth in the Four Corners region and suggests sound taxation policies that could be used to capture much of the value of the extraction that is going to take place.

The final report will refine these preliminary taxation thoughts and explain how increased revenues should be used in support of growth that will be necessary for a sound state economy when the resources run out.

1. Revenue Potential from Mineral Wealth

The Four Corners region is blessed with immense mineral resources. The annual value of regional mineral production should exceed $13 billion by 1981 (see Table 5 attached). First in resource wealth is New Mexico, with annual production estimated to reach $5.5 billion, or about $ 400 per capita. Arizona, Colorado, and Utah produce approximately $2½ billion each, for annual per capita revenues of $1,100, $900, and $1,700 respectively. Nevada's output of $600 million is about $850 per capita.

The region's resource endowment is richly diversified, as oil, natural gas, coal, uranium, copper, molybdenum, gold and other mineral deposits provide an impressive source of wealth. Each state, however, has its own unique combination of mineral assets (see table 3), the most important of which are summarized below:

Arizona: Arizona produced some 65% of the nation's copper in 1979.[1] Significant amounts of molybdenum, silver, gold, and other minerals were produced both as co-products of copper production, and on their own. Energy production, with the exception of coal, was relatively modest in the region.

Colorado: The leading mineral produced in Colorado, in terms of value, is oil. 1981 production of approximately 29 million barrels will gross $1 billion in sales. Second in importance are the two fabulously wealthy molybdenum mines owned and operated by AMAX. 1980 output of 102 million pounds amounted to nearly one half of all non-communist production, and more than enough to supply the entire U.S.[2] The flagship of Colorado molybdenum producers is the "incredibly productive . . . Climax molybdenum mine . . . known in mining circles as the eighth wonder of the world."[3] The Climax mine, in production since 1918, has recently been joined by the vast Henderson mine, reported to be the largest single business venture in the history of Colorado.[4] The combined sales from these two mines alone is estimated at $900 million in 1981, providing AMAX with its most important profit center. In addition to its main products of oil and molybdenum, Colorado produces respectable quantities of natural gas and coal, as well as a number of other metals.

New Mexico: Richest of the states in the Four Corners region, New Mexico enjoys substantial oil production ($2.2 billion), natural gas ($1.6 billion), and is the nation's largest producer of uranium "yellowcake" ($220 million in U_8O_2 production).[5] Coal production for 1981 is estimated at 20 million tons. In addition to its considerable energy resources, New Mexico produces about $300 million in copper and is the nation's leading producer of perlite and potassium salts.[6]

Nevada: With the opening of the Jerritt Canyon mine, Nevada will become the nation's largest producer of gold.[7] Ninety-nine percent of the domestic production of mercury is produced in Nevada, and it is the major supplier of barite. The new Anaconda mine near Tonopah is expected to produce some 15 million pounds of molybdenum by 1981, equivalent to 5 percent of "free" world consumption. Copper production in Nevada has undergone a drastic decline in the wake of falling copper prices.[8]

Utah: Blessed with rich oil, coal, and uranium deposits, Utah is an energy-rich state. Kennecott operates the largest open pit copper mine in the world in Bingham, and total copper production in 1979 ranked second in the nation. Utah also is a leading producer of gold and beryllium.[9]

This great wealth is a major source of tax revenue for the Four Corners region, although to date no systematic effort has taken place to assess the full revenue potential of the resources, particularly in light of important changes in tax policies in other resource-rich countries around the world.

The revenue potential from mineral development is determined by evaluating a complex set of factors beyond simply the gross value of in-state production. Changes in technology, industry market structure, ore grades, "the depth of the ore below the earth's surface, its shape and continuity, and the properties of the host rock formation"[10] all figure in determining the "economic rent"* from a particular mining venture.

Thus, for example, an initial "back of the envelope" review of Four Corners' production suggests that taxes on oil production could, potentially, raise more than $1.1 billion dollars annually over the present state "take," and $100 to $250 million in annual revenues could be raised from molybdenum production, if firms operating in this region paid taxes comparable to those levied internationally. Natural gas and coal also provide significant opportunities for increased mineral tax revenue.

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*Economic rent is an important concept in mineral taxation. It refers to the returns which are in surplus of that required to attract capital and other factors of production. Thus, a properly designed tax policy should attempt to capture these "rents" while causing the least reduction of investment in the development of the resource.

On the other hand, the uranium industry is currently suffering from weak demand, in the wake of slowdowns in nuclear development and a legal attack on the international uranium cartel. Likewise, copper prices are currently at less than 65% of last year's peak prices, and competition from rich deposits in Africa and Chile has reduced the profitability of U.S. operations.

There is a great divergence in each state's approach to mineral taxation. On the one extreme is Nevada, whose tax policies were recently praised by an Anaconda official:[11]

> It should be no surprise . . . that Nevada was the low state. Nevada does not have a severance tax or a state income tax. I've always said that if ore bodies had wheels, I'd move all our mines to Nevada.

None of the other states has demonstrated an aggressive approach to capturing mineral "rents," with the possible exception of the New Mexico uranium tax that ties its marginal tax rate to the price of yellowcake.[12] The top severance tax on oil and gas production is 6.3%, also in New Mexico, a rate that has changed little since 1969.[13] The Colorado tax on molybdenum production is only 15¢ per ton of ore, the equivalent of less than one quarter of one percent of the value of the mineral output at current prices.[14]

Corporate income taxes range from a high of 10.5% in Arizona, to 5% in New Mexico and Colorado, 4% in Utah, and zero in Nevada. The effective rate of the Arizona tax is overstated, however, as federal income taxes are allowed as a deduction. Colorado and New Mexico use the federal tax base to determine net income, and both allow percentage depletion allowances for most minerals, thus lowering the firm's effective tax rate by more than one-half in most cases.[15]

Mine property taxes are an important source of revenue in the Four Corners region, although assessment practices vary widely. Arizona uses a five-year average of historical profits to estimate the present value of a mine. Nevada limits its tax base to a year's net proceeds, while New Mexico uses a variety of bases, including 9% of annual production (oil), 25% of gross value less royalties (uranium), and profits (coal and other minerals). Utah uses an average of past net proceeds, and it also requires new mines to prepay taxes to offset increased demands on public services. Colorado allows a share of local property taxes as a credit against state severance taxes on metals and oil and gas production, thereby reducing the effective tax burden on the industry.[16]

2. Designing a Mineral Tax Strategy

In designing a state taxation strategy, it is important to consider the advantages and disadvantages of different revenue tools. Taxes based on the gross value of mineral production not only fail to discriminate between the profitability of different minerals, but also neglect the profitability of different mines producing the same mineral. Moreover, different types of taxes tend to have regulatory or distorting impacts that change mining operations and, in some cases, result in less efficient recovery of mineral resources. For example, severance taxes cause "high grading" of ores--which is an increase in the minimum mineral content necessary for profitable mining--and provide incentives to delay mineral production. Property taxes, on the other hand (and depending upon the method of assessment), provide incentives to escalate production rates. The federal (and, when allowed, the state) percentage depletion allowance is like a reverse severance tax, creating incentives for "low grading" of deposits, and speeding up development.[17]

Different taxing tools also influence the risks of mineral development. Property and severance taxes discourage exploration efforts because the rewards of discovery are reduced while the costs of exploration remain unchanged. Severance taxes must be paid regardless of the profitability of the mine and thus increase the downside risk of operations. Taxes on net income share in the risks of exploration and changes in profitability and may actually increase the risk-taking behavior of investors.[18]

Finally, government revenue needs and practical administrative problems influence taxing strategies. Property and severance taxes generally provide a steady source of income and may even be paid prior to production to finance early infrastructure development. Net income taxes, on the other hand, vary widely from year to year if mineral prices are unstable. Severance taxes are the easiest to administer, and this reason alone may explain their popularity. Property taxes are relatively easy to assess against oil and gas reservoirs, but much more controversial when applied to hard rock mining deposits.[19]

Taxes on net income are more complex due to the difficulties of taxing multistate corporations and determining the proper allocation of profits among groups of affiliated subsidiaries.[20]

In general, a state with modest taxing goals may find the severance tax approach preferable. In addition to the ease of administration, the tax enjoys some political acceptance, and tax rates may correspond to the rough measures of the costs that development imposes or the policy makers concept of the public "equity" in the resource.

For more ambitious taxing efforts, states are well advised to consider more sophisticated methods of capturing economic rents from mining activity. Over the past ten years there has been a virtual revolution in worldwide government fiscal policies toward mineral deposits, leaving most U.S. state policies primitive by comparison. Important models for aggressive taxing strategies exist as geographically close as Canada and the city of Longbeach, California, and as culturally close as the British North Sea. Recently negotiated agreements between major U.S.-based mineral corporations and the governments of Papua-New Guinea, Indonesia, Malaysia, Norway, and The Netherlands provide valuable yardsticks of the industry's ability to share the wealth from mineral development.

Experience has shown, here and abroad, that successful taxation strategies must be based on a keen understanding of the technical and economic aspects of each state's mineral industry. Careful attention must be given in each state to building data bases, and the construction of models which can inform policy makers of the impact that tax policies have on the profitability of the mining sector. For this purpose, it is recommended that states develop capabilities for evaluating tax policies using the Discounted Cash Flow (DCF) rate of return method, which is widely used in the industry itself.[21] In the absence of independent analysis, policy makers are likely to accept uncritically industry assertions regarding the economic impacts of taxation policies.

Finally, it is very important that states provide a clear and well-understood plan for investing new revenues. Programs for spending or investing resource wealth are helpful both in defining state development goals, and rallying public support in the face of frequently bitter industry opposition to increased tax payments. Tax proposals which link revenues to spending or investment strategies are less likely to be perceived as anti-growth or anti-development. In a very real sense, the cost of imposing the tax is compared to the benefits from the revenues. The potential benefits, made tangible by such a plan, are thus the opportunity cost of foregoing new tax proposals.

3. Taxes on Copper Production in Arizona

Arizona is the largest producer of copper in the United States. 1979 output was equal to two-thirds of U.S. and one-eighth of world copper production. As an independent country, Arizona's copper production would rank second in the world, behind Chile, based on 1979 output.[22] Compared ot other leading producers, such as Australia, Zaire, and Zambia, Arizona copper is produced from low-grade ores, averaging .49% copper content in 1978.[23]

Prices have been erratic in the past several years, ranging from $.66 per pound in 1978, to more than $1.30 per pound in February 1980, to approximately $.85 per pound in June of 1981.[24]

The "economic rent" from Arizona's copper production is hard to estimate from any one year's price and production statistics, as the economic viability of mining enterprises is a function of prices over time, and the individual characteristics of particular mines. Arizona's present tax structure, consisting of a corporate income tax, local ad valorem property taxes, and a modest 2.5% severance tax, yields total returns typical of tax levels in many other states. It is considerably lower than returns found in many foreign jurisdictions which are mined by the same companies that are active in Arizona. For example, in British Columbia the government's tax on production of metallic minerals is 17.5% of net proceeds, plus a corporate income tax of 15%, for a combined "take" of approximately 30% of net proceeds.[25] In addition, the firm is liable for federal income taxes. Other foreign governments employ a variety of income and excess profits taxes to allow the firm to earn reasonable profits while the state captures extraordinary earnings. In some cases this is accomplished through an overpricing scheme, where an excise tax is levied against the portion of the selling price which exceeds a basic "floor" price.[26] More recent efforts to "skim economic rents" are based directly on the mining operation's return to capital. For example, both Peru and Papua-New Guinea base the top marginal tax rate on the firm's Discounted Cash Flow (DCF) rate of return.[27] This later approach is recommended as a supplement to the existing Arizona tax structure.

In other words, mines would pay the basic property and corporation income tax that other firms pay. In addition, the 2.5% severance tax would insure that some minimum payment is made to compensate for environmental impacts and the depletion of renewable resources. Finally, a special income tax, based on the firm's return to capital, would insure that the citiznes of Arizona benefit from windfalls from escalations in the world price of copper, or development of extra rich deposits which yield returns greater than that required to attract capital investment.

INFORMATION FOR TANDEM LOAN APPLICATIONS

1. DEFINITION: Tandem loans refer to a single loan application for a Guaranty Participation AND a Direct SBA loan, the approval of each loan being contingent upon approval of the other.

2. ELIGIBILITY: Any existing business or "start-up" which evidences a thin equity position but is otherwise considered to be a viable entity from the standpoint of profitability, feasibility, and having an economic importance, such as job creation, etc., may be considered. Firms owned or to be owned by racial and ethnic minorities or women, regardless of race or ethnicity which evidence an insufficient equity base to allow a bank to participate in a Guaranty or to make a Direct bank loan are candidates. The SBA Direct loan is to be considered, by virtue of its terms, to be long term capital, hence a form of equity.

3. TYPE AND AMOUNT OF LOANS:

   a. The SBA Direct loan may not exceed $100,000.

   b. Aggregate of SBA's Direct loan and its share in the Guaranty Participation loan may not exceed $500,000.

   c. SBA's Direct loan in any application will not exceed 25% of the total loan amount needed.

   d. Bank's Guaranty Participation loan will be the amount required after deducting SBA's Direct loan amount from the total financial requirement.

4. COLLATERAL REQUIREMENTS:

   a. All business assets, personal guarantys, residential equities, intangibles, etc., will be subject of lien.

   b. Participating bank to have senior lien position on all business assets to secure its participation loan.

   c. SBA to have subordinated lien position on same assets.

   d. Collateral values securing SBA loan, either existing or to be acquired, shall be sufficient to reasonably protect the interests of the Government.

5. CREDIT REQUIREMENTS: Applicants evidencing a need for tandem financing will generally report Net Worths (including amounts owed to owners which can be subordinated) less than the "mean" ratio for businesses of like size and type as stated in RMA financial statement statistics. Minimum net worths caused by successive operating losses but which are being improved by a profitable trend should be assisted by "tandem" financing. Repayment ability must be evident for the combined financing. The SBA Direct loan may be subject to a deferment of principal only for the first year of term only.

6. PROCESSING AND DISBURSEMENT: The bank will submit a single loan application package on behalf of the applicant, indicating its credit review of the total financing, i.e., direct and guaranty, and indicate its approval as in any Guaranty participation. The bank will also include in written form that the amount of Direct loan financing involved is unavailable from the bank and that the entire financing could not be approved without the use of Direct SBA loan funds due to poor equity and for other reasons.

   The SBA Direct loan will be disbursed after the bank evidences disbursement of its loan to the borrower.

May 1, 1981

NOTES TO SECTION IV

[1] Minerals Yearbook, 1978-79 (U.S. Bureau of Mines).

[2] Karl E. Starch, "The Mineral Industry of Colorado," 1978-79, Minerals Yearbook, 1978-79 (U.S. Bureau of Mines).

[3] Michael Tanzer, The Race for Resources (Monthly Review Press, 1980), p. 166.

[4] Starch, op. cit.

[5] Production of U_3O_8 (yellowcake) dropped by nearly 50% over the past two years as prices have declined in the wake of reduced demand and legal attacks on the international uranium cartel.

[6] Robert H. Arndt and Robert W. Eveleth, "The Mineral Industry of New Mexico," Minerals Yearbook, 1978-79.

[7] John Schilling, "Nevada's Mineral Industry: An Update," Nevada Review of Business and Economics (Winter 1980-81), p. 6.

[8] Ibid.

[9] Lorraine B. Burgin, "The Mineral Industry of Utah," Minerals Yearbook, 1978-79.

[10] Tanzer, Race for Resources, pp. 42-43.

[11] C. J. Hansen, "If Cabbages Were Kings--A Practical Approach to the Taxation of Mining Properties," included in Albert Church Editor, Non-Renewable Taxation in the Western States (Lincoln Institute of Land Policy and College of Mines at the University of Arizona, 1977).

[12] In 1981 the New Mexico legislature reduced the uranium severance tax for the next three years by providing that the tax will be based on 60 percent of the price of yellowcake. Chapter 169, SLA 1981.

[13] The 6.3% rate includes both the severance and the emergency school tax.

[14] Based on current ore grades in Climax and Henderson mines.

[15] Although percentage depletion allowances have generally been phased out for most oil and gas producers, it survives for most minerals. According to Peter C. Maxfield, The Income Taxation of Mining Operations (Rocky Mountain Mineral Law Foundation, 1975), the following rates are still in effect:

Percentage Depletion Rates

22%	Sulfur, uranium, plus U.S. deposits of bauxite, fluorspar, lead, mercury, molybdenum, nickel, tin, tungsten, zinc, rutile, clay, mica, and many more minerals.
15%	U.S. deposits of gold, silver, copper, iron ore and oil shale.
14%	All other metal mines and refractory clays plus nearly all other minerals not elsewhere accounted for, ranging from potash to oyster shells.
10%	Coal, lignite, perlite, salt, brucite, wollastonite, and some asbestos.
7½%	Sewer pipe clay, and clays, slates, and shales used as sintered lightweight aggregate.
5%	Sand, gravel, peat, pumice, stone, and other industrial minerals.

[16] Robert F. Conrad and R. Bryce Hool, Taxation of Mineral Resources (Lexington Books, 1980).

[17] For an accessible discussion of the high grading problem see Conrad and Hool, Ibid.

[19] For a discussion of this principle, see Richard Musgrave, The Theory of Public Finance (McGraw-Hill, 1959), chapter 14.

[19] Robert H. Paschall, "What Are Our Real Goals in Mineral Taxation," included in Church, ed., Non-Renewable Taxation in the Western United States.

[20] Charles E. McLure, Jr., "The State Corporate Income Tax: Lambs in Wolves Clothing," included in Henry J. Aaron and Michael J. Boskin, editors, The Economics of Taxation (the Brookings Institution, 1980), pp. 327-348, and Gene Corrigan, "Toward Uniformity in Interstate Taxation," Tax Notes (September 15, 1980).

[21] The discounted cash flow rate of return method gained wide acceptance in the mineral industry from the 50s on. The DCF method takes full account not only of the size of profits and investments, but also the timing of cash flows. Thus, the DCF method of measuring profits has important advantages for mining projects, which have long lead times and duration. One economist has explained the calculation as follows:

> The DCF profit rate is calculated from the net cash flows by finding an implicit interest rate such that, if the money used for the exploration and development investment had been put in a bank instead (at that same interest rate), the amount of money accumulated in the bank at the end of the life of the oil field would be equal to the total amount of money accumulated from the actual oil investment (assuming that the actual net cash flows from oil production had been also reinvested each year at that same interest rate).

Quote taken from Michael Tanzer, "Negotiation Strategies and Objectives in Petroleum Exploration and Development Agreements: The Host Governments," paper presented at the United Nations Meeting on Petroleum Exploration Strategies in Developing Countries (The Hague, The Netherlands, 16-20 March 1981).

[22] *Minerals Yearbook, 1978-79* (U.S. Bureau of Mines).

[23] James H. Jolly, "Copper," ibid.

[24] 1978 and 1980 price quotes from *Minerals and Materials* (U.S. Bureau of Mines, October 1980). 1981 price quote from March 30, 1981 issue of *Business Week*.

[25] Interview with mineral taxation officials, June 1981.

[26] Examples would include the Chile "overprice" scheme of 1969, which required graduated excise taxes as the price of copper exceeded $.40 per pound. The top tax rate as 70 percent of the "excess" over $.70 per pound. In the Philippines a tax of 30 percent of the excess over a "basic export price" is used, which was $.90 per pound in 1979.

[27] Firms active in Peru and Papua-New Guinea include AMAX and Amoco.

Table 5

Value of Mineral Annual Production in the Four Corners Region

Mineral	Quantity	Price	Value of Production
	Arizona		
copper	946,002 mt. tons[1]	$.85/lb.[2]	$1,773
molybdenum	35.1 million lbs.[1]	$9.00/lb.[3]	316
silver	7,479 thousand troy ounces[1]	$11.00/oz.[4]	82
other non-fuel			254[1]
oil	471 thousand barrels[5]	$35.00[6]/lb.	16
gas	348 mmcf[5]	$1.50[3]/mcf	.5
coal	11.4 million tons[5]	$20.00[7]/ton	228
			$2,670
	Colorado		
oil	29,565 thousand barrels[8]	$35.00/lb.[6]	$1,035
gas	192,931 mmcf[5]	$1.50/mcf[9]	289
coal	14.3 million tons[5]	$20.00/ton[7]	286
uranium	950 million tons[5]	$22.00/lb.[10]	42
molybdenum	102 million lbs.[11]	$9.00/lb.	918
other non-fuels			140[1]
			$2,710

Value of Mineral Annual Production in the Four Corners Region (cont.)

Mineral	Quantity	Price	Value of Production
	Nevada		
oil	880,405 barrels[8]	$35.00/lb.[6]	31
gold	405,618 troy oz.[12]	$480.00/oz.[13]	216
barite	2,268 tons[14]		62[14]
molybdenum	15 million lbs.[15]	$9.00/lb.[3]	135
mercury	33,000 76-lb. flasks[14]	$425.00/flask[13]	14
other non-fuel minerals			140[14]
			$ 598
	New Mexico		
oil	62,780 thousand barrels[8]	$35.00/lb[6]	$2,197
gas	1,132 mmmcf[16]	$1.50/mcf[9]	1,588
gas liquids			300[17]
coal	20 million tons[18]	$20.00/ton[7]	400
uranium	5,000 tons U_3O_8[19]	$22.00/lb.[10]	220
copper	164,281 metric tons[1]	$.85/lb.[2]	308
potassium salts	2,005,000 mt. tons[1]		229[1]
other non-fuel minerals			128[1]
			$5,370

Value of Mineral Annual Production in the Four Corners Region (cont.)

Mineral	Quantity	Price	Value of Production
	Utah		
oil	31,025 thousand barrels[8]	$35.00/lb.[6]	$1,086
gas	84,578 mmcf[20]		80[20]
coal	13.6 tons[20]	$25.00/ton[20]	340
uranium	1,000 tons U_3O_8[20]	$22.00/lb.[10]	44
copper	153,223 metric tons[14]	$.85/lb.[2]	287
gold	190,000 troy ounces[14]	$480.00/oz.[13]	91
silver	2,036,000 troy ounces[14]	$11.00/oz.[4]	22
other non-fuel minerals			242[14]
			$2,192

TOTAL	Arizona	$2,670
	Colorado	2,710
	Nevada	598
	New Mexico	5,370
	Utah	2,192
		$13,540

NOTES TO TABLE 5

[1] 1979 production as reported by the U.S. Bureau of Mines, in the 1978-79 Minerals Year Book.

[2] May 30, 1981 quote of copper prices, as reported in Business Week, June 15, 1981.

[3] 1980 price as quoted in Minerals and Materials, a Monthly Review (U.S. Department of the Interior, October 1980).

[4] Average of recent market quotes as reported in Wall Street Journal (June 2, 1980).

[5] 1979 production, as reported in Ronald L. McMahan and Porter B. Bennett, "Energy Activity in the West" (ABT/WEST and WESTPO, March 1981).

[6] Estimated 1981 price.

[7] In Colorado state officials estimate that steam coal, which represents about 85% of production, sells for $20 to $25 per ton at the mine, while metallurgical prices are significantly higher. According to Louie Martinez, of the New Mexico Department of Energy and Minerals, large portions of New Mexico coal are sold under long-term supply contracts at low prices, or are produced from "captive" mines. Newer production is selling for as much as $30 per ton, although competition from Wyoming suggests that a price of $20 to $25 is reasonable. Utah alone among the Four Corners states produces all its coal from underground mines. According to Martha Smith, of the Utah Department of Natural Resources, prices are estimated in the $23 to $26 range for most production, which is a low grade anthracite. Prices in Arizona and Nevada were assumed to parallel the other states.

[8] 1981 estimate based on daily production as reported in Oil and Gas Journal (April 13, 1981).

[9] 1980 estimated price as reported in 1980 AMAX Annual Report.

[10] Uranium prices are estimated by Bill Hatchell, staff geologist for the Bureau of Geology, New Mexico Department of Energy and Minerals; and Martha Smith, Utah Department of Natural Resources.

[11] 1980 production as reported in 1980 AMAX annual report.

[12] Represents combined 1980 production of 250,000 oz. plus 200,000 oz. from start-up of Jerritt Canyon Mine. 1980 production estimates provided by U.S. Bureau of Mines. Jerritt Canyon Mine Production estimate provided by John Schilling, "Nevada's Mineral Industry: An Update," *Nevada Review of Business and Economics* (Winter 1980-81), p. 6.

[13] *Wall Street Journal* quote (June 2, 1980).

[14] U.S. Bureau of Mines preliminary estimate for 1980.

[15] Estimated 1981 production given in Joyce Hall and John Schilling, "The Nevada Mineral Industry, 1979" (Nevada Bureau of Mines and Geology).

[16] 1980 production, as reported by D. Donaldson, April 3, 1981, based on data from the New Mexico Oil Conservation Division.

[17] The value of gas liquids production is estimated on the basis of 1978 values, as reported in "Minerals in the Economy of New Mexico" (U.S. Bureau of Mines, 1979).

[18] 1981 production estimate provided by Louie Martinez, Bureau of Geology, New Mexico Department of Energy and Minerals.

[19] 1981 estimate provided by Bill Hatchell, Bureau of Geology, New Mexico Department of Energy and Minerals.

[20] Estimates provided by Martha Smith, Utah Department of Natural Resources.

THE WHITE HOUSE
CONFERENCE ON SMALL BUSINESS

JANUARY 13-17, 1980

ISSUE PAPER
CAPITAL FORMATION AND RETENTION

SEND COMMENTS TO: Michael K. Casey, Director
Research & Policy Development
712 Jackson Place, N.W.
Washington, D.C. 20006

EXECUTIVE ORDER

By the authority vested in me as President by the Constitution and statutes the United States of America, and in order to establish procedures that eliminat all paperwork burdens on the public above the minimum necessary to determine and implement public policy and ensure compliance with Federal laws, it is hereby ordered as follows:

1-101. Agencies shall minimize the paperwork burden -- i.e. the time and costs entailed in complying with requests for information and recordkeeping requirements -- imposed on persons outside the Federal government. Forms should b used only to the extent necessary to gather the basic information required to fulfill an agency's mission. When forms must be used, they should be as short a possible and should elicit information in a simple, straightforward fashion.

1-102. Each agency shall designate an existing official to be responsible for minimizing both the agency's use of forms and the paperwork burden resulting from proposed legislation and regulations.

1-103. Agencies shall pay particular attention to the special burdens face by individuals and small organizations in responding to requests for information. To minimize these burdens agencies should, whenever possible, forego uniform or universal reporting requirements and rely instead on sampling, reduced frequency reporting, differing compliance standards, or exemptions.

1-104. Each agency shall prepare an annual paperwork budget, i.e. an estima of the total number of hours required to comply with requests for informatio budget should itemize each form used, describe its purpose and identify those affected by it. The Director of the Office of Management and Budget shall review a may modify each agency's proposed budget. After the Director has approved an agency's paperwork budget, it may be increased only by the Director upon request of the head of the agency.

1-105. Forms or similar requests for information shall be reviewed within t years after their initial issuance and then at least once every five years. Foll ing review, they should be revised or abandoned to the extent they are not requir to meet an agency's basic information needs. These reviews will be conducted by the agencies, and reports of the reviews will be submitted to the Director.

1-106. The Director shall audit compliance with this Order and may issue rules and regulations necessary to implement it. The Director may issue exemptio for agencies whose use of forms is limited. The Director also shall:

(a) Seek to eliminate duplication in requests for information by establishing a Federal information locator system, which will list all the types of information collected by Federal agencies and will be available for use by all agencies. This or similar systems will not contain any information obtained from the public. The Director shall take any other steps needed to prevent duplication, including the assignment to a particular agency of lead responsibility for the collection of certain types of information.

(b) Seek to inform the public and broaden public and agency comment by preparing and publishing in the *Federal Register* an annual paperwork calendar of significant requests for information. This calendar will be based on the information contained in the agencies' paperwork budgets.

(c) Report annually to the President on implementation of this Order and control of the paperwork burden generally.

1-107. The authority vested in the Director under this order shall not affect any authority vested in him by any other Order. This Order shall be implemented in a manner consistent with all applicable Federal statutes.

1-108. For purposes of this Order, agency means those agencies covered by Executive Order 12044.

1-109. This Order will expire on September 30, 1983.

Jimmy Carter

THE WHITE HOUSE

November 16, 1979

FOR IMMEDIATE RELEASE NOVEMBER 16, 1979

Office of the White House Press Secretary

THE WHITE HOUSE

The President today directed executive departments and agencies to ensure that their regulatory programs, while achieving their goals, do not place unnecessary burdens on small businesses and organizations.

This action followed his decision on October 31 to add the Small Business Administration to the Regulatory Council in order to strengthen that Council's capacity to meet the concerns of small business.

The President expressed his appreciation to Senators John Culver and Gaylord Nelson and Congressmen Andy Ireland, Marty Russo and Neal Smith, sponsors of specific small business legislation now before Congress, for their leadership in helping America's small business men and women.

The President's memorandum to department and agency heads today directs them to take the following steps:

--Ensure that new regulations take into account the size and nature of the regulated businesses while achieving intended social and economic goals of regulations.

--Determine where existing regulatory and reporting requirements can be tailored to fit the size and nature of the businesses and organizations subject to them.

--Identify those rules and regulations in the semiannual agenda required by Executive Order 12044, and in the Regulatory Council's Calendar of Federal Regulations, for which flexible alternatives are being considered.

--Report the results of this process to the Office of Advocacy of the Small Business Administration by December 15.

The review of existing rules and development of implementation plans will be undertaken with the assistance of the Regulatory Council and the Office of Management and Budget. All actions under the directive must be consistent with the laws under which the agencies operate.

The President also sent a letter to the heads of independent agencies today requesting that they consider a similar review of existing and new regulations within their agencies.

# # #

PREFACE

This paper is one of a series prepared for the White House Conference on Small Business. Along with the others, it reflects issues and recommendations that emerged from a year and a half process that involved over 30,000 business owners in every state.

Nothing in these papers should be considered recommendations or policy statements by the Conference Staff, the White House, or any Federal agency. Rather, the commentary, options and discussion are intended to identify for Conference delegates the major issues and recommendations that emerged from the field meetings, task force deliberations and delegate caucuses, and to provide a framework for deliberation at the Conference.

INTRODUCTION

As any small business person knows, the cost of capital and its availability to business determines, perhaps more than any other single factor, whether that business will succeed in its start-up years. After a business is established, capital availability also plays a large role in determining whether it will be able to grow according to its owner's desires and expectations.

Many factors affect a small business' ability to obtain and retain capital. These include: the tax code, the structure of the debt and equity markets, federal programs for the distribution of loan guarantees or direct financing, as well as the overall economic condition of the nation. Particularly for the small business sector of the nation's economy which is first to feel the impact of unfavorable economic conditions, the ability of a business to retain earnings will be crucial in determining the amount of profit the owner will take away from the business as well as the amount left over to finance growth.

All businesses differ, but in its economic "life cycle" a small business may need different kinds of financing at different times. While some financial matters are of concern to nearly all business owners and others are less important, it is important that access to all types of financing be readily available to the nation's small business sector in order that it retain the capability to grow, at a reasonable rate, to the size it desires.

Tax Policy

Tax policy provides the single most important mechanism for encouraging the flow of capital into sectors of the economy, such as the small business sector, which, because of problems in the financial markets or other external pressures, might otherwise receive less effective financing.

Erosion of retained earnings by corporate over-taxation can materially inhibit small business expansion, particularly in light of the difficulties often faced in obtaining adequate external capital. Although corporate tax rates have historically been graduated, inflation has more than doubled price levels in the past few decades forcing firms into higher tax brackets.

Largely because of their vulnerability to inflation, depreciation schedules imposed by the I.R.S. are another important potential tax drain for small businesses.

Small businesses, like all firms, face higher effective tax rates when depreciation of assets at historical costs underestimates replacement costs, thereby exaggerating reported profits.

Whatever the income tax laws, retained earnings often will be inadequate to support growth during a firm's early stages forcing it to rely upon external funds for financing growth. Income taxes levied upon investors in small business are another area of taxation that can have significant impact upon the attractiveness of small business investment to outside investors. Perhaps most significant is the treatment of capital gains realized on the sale of small business equity holdings, since young growth companies rarely pay significant dividends during their early years, offering instead the potential for capital appreciation.

Increases in the capital gains tax are widely blamed in many segments of the business community as having a chilling effect upon activity in the venture capital and new issue markets. Increased capital gains taxes alter risk/reward relationships, to the detriment of growth-oriented equity investments.

Debt Capital

Commercial Banks

Commercial banks and finance companies are by far the most important sources of small business financing, since short and intermediate term credit for the support of inventories and receivables is often a small business's primary financing need. Much of the lending done by commercial bankers, particularly for new firms, is done on a secured basis. In the short-term area, it includes the financing of inventories and accounts receivable. Intermediate-term lending often takes the form of installment credit for the purchases of equipment. Longer-term debt financing for small business is available largely in the form of commercial and industrial mortgages from banks and life insurance companies.

Life Insurance Companies

Life insurance companies' unsecured lending to small business is quite limited. Few insurance companies possess the extensive network of field offices that is needed to facilitate the handling of small non-mortgage loans, and most find it more economical to place large blocks of funds. While several insurers have expanded their regional lending through "small business" departments, these departments are directed primarily at intermediate sized companies with assets of between $5 to $100 billion. Insurance companies are not geared toward high-risk loans but rather to established companies with an earnings record of at least several years. Nevertheless, insurance companies are a significant source of 10 to 15 year loans to some smaller companies.

Savings and Loan Banks

Savings and loan companies are chartered to attract savings deposits from the general public and to make loans secured by first liens on real estate in order to enable borrowers to purchase, refinance, construct or improve properties. Federal law permits savings and loan associations to make commercial real estate loans, but, funds are available for "bricks and mortar" secured by a first mortgage only. No more than 75% to 80% of appraised value can be advanced. If the property is to be used for unusual or special purposes, (i.e., a bowling alley, disco, mortuary, etc.) financing is even more difficult to obtain from this source.

Recent Trends in Banking Regulation Affecting Small Business Lending

Some observers of bank allocation of credit anticipate that the recently enacted Community Reinvestment Act (CRA) will have a significant effect upon all kinds of lending institutions' willingness and ability to make small business loans. Briefly, the Act requires the financial regulatory agencies of the federal government to determine whether the regulated financial institution is acting in the best interests of the community. Although all banking regulators are in the early stages of reorganizing their agencies to meet the requirments of the Act, most have indicated that they plan to look beyond the obvious issues of redlining or sex discrimination, to more complex and sophisticated concepts of how to convert some consumer lending activities to generate more competitive business lending.

Equity Capital

Venture Capital

The start-up capital for a small business is most often contributed by the would-be business owners savings, or by friends or relatives. A rapidly growing new business, however, can quickly exhaust these funds and may need additional outside risk capital. Venture capital is the name given to private financings which provide this necessary risk capital until a company has matured to the point where it can arrange a public stock offering.

In the most common form of venture capitalism, investors purchase a minority interest in a growing firm, with the goal of recouping the investment after helping the company arrange a public stock offering within several years. These investments are generally very high-risk, with a potential for equally high return. Technology-based firms are major recipients of venture capital because investors seeking growth potential are attracted to new projects in industries experiencing a rapid rate of technological change.

Small Business Investment Companies

Small business investment companies (SBIC's), are privately-owned firms licensed by the SBA to provide equity and long-term loans to small business. SBIC's are eligible to receive long-term SBA-guaranteed loans from the Federal Financing Bank at interest rates 1/8 of 1 per cent above the cost of funds to the Treasury. They enjoy advantageous tax treatment and SBIC shareholders are permitted to deduct any capital losses suffered on the sale of SBIC stock as ordinary income.

SBIC investments range from straight loans, to common equity in small business. The SBA sets size standards determining a firm's eligibility for SBIC financing, and insists that loans be of at least 5 years maturity. SBIC's tend to be most active in providing expansion capital to established businesses. As a group they pursue more conservative investment policies than other venture capital firms and are less active in financing early-stage, high technology enterprises.

SBIC's generally place greater emphasis than other venture capitalists upon income-generating investments such as convertible debentures and straight long-term debt. Straight loans accounted for roughly 38 per cent of outstanding SBIC business investments in 1973, with an additional 28 per cent in debt with equity features and the remaining 34 per cent in pure equity. This lack of emphasis upon equity investment has been a frequently criticized aspect of the SBIC program, particularly in light of the fact that debt financing is generally available from other sources.

Public Offerings

With debt financing limited by a company's equity base, new equity or risk capital must be obtained if the life cycle of the company is to proceed without interruption. The longer a firm is in business, the more successful it is, and the larger its equity base, the easier it is for it to fill its financing needs. As a result, smaller, developing companies, which need capital most, experience the greatest difficulty in obtaining it.

The ability of small business to obtain equity financing has always been a difficult problem. For example, of the $6.4 billion raised via common stock offerings in 1977, only $207 million, or 3.2 per cent of the total, was raised by companies offering securities to the public for the first time. The share of the dollar value of securities offered through smaller issues to the public has remained relatively constant over the last five years.

Public financing is not normally available to a company until it has achieved a minimum of $10 million in revenues. This has not always been the case. In recent years, there has been an upward shift in the amount of revenue needed before a public offering can occur. This increased need for revenue is due in part to inflationary pressures, but also reflects real increases in fees for accountants, attorneys, printers and others who participate in the preparation of a new issue.

OPTIONS

Option 1

Replace the present income tax schedule with a more graduated rate scale, and index the tax schedule for inflation.

Discussion

Corporate Taxes

Until January 1, 1979, the first $25,000 of corporate income was subject to a tax rate of 20%, and the second $25,000 was taxed at a rate of 22%. All corporate taxable income in excess of $50,000 was subject to a surtax of 26%. Thus, all taxable income in excess of $50,000 was subject to a tax rate of 48%.

In 1978, the tax writing committees of Congress determined that the rapid rate increase from 22% to 48%, constituting a 118% jump, imposed a detrimental tax burden. Accordingly, Congress repealed the existing corporate tax and surtax structure, and in its place imposed a 5-step rate structure on corporate taxable income as follows:

Taxable Income	Tax Rate
$ 0 - 25,000	17%
$25,000 - 50,000	20%
$50,000 - 75,000	30%
$75,000 - 100,000	40%
Over $100,000	46%

The philosophy of a graduated income tax is that it allows small and medium size companies to plow back a greater portion of earnings into their businesses for necessary expansion and improvements. A graduated rate structure distributes tax benefits among small and medium sized firms more evenly than the former tax and surtax system. Thus, the small and medium size businesses, which comprise about 97% of all U.S. enterprises, may retain more of their profits and thus fuel their own growth. Since equity financing is extremely difficult for small firms and debt financing can be prohibitively expensive during periods of high interest rates, a graduated corporate income tax rate structure allows small corporations to retain additional earnings and thereby plan their growth logically and execute their plans more efficiently.

Congress has accepted the concept of a graduated corporate income tax rate structure. What remains at issue, however, is the upper limits of the tax brackets. As noted above, the present corporate rate structure imposes a maximum tax rate on income levels above $100,000. Capital formation would be enhanced by raising the top bracket to shift greater amounts of capital to the small and medium sized businesses which create more jobs than the large corporations.

The primary objection to this increase is that substantial tax revenues would be lost. Such revenue losses would vary depending on the bracket structures adopted. On an absolute basis, disregarding any benefits to the U.S. Treasury from additional job creation, capital investment and increased productivity, the 1978 changes in the corporate rate structure were estimated to have cost the U.S. Treasury $5 billion in 1980 alone.

The ten regional caucuses produced various proposals for graduated corporate taxation. Delegates proposed raising the present $100,000 ceiling to amounts ranging from $200,000 to $1,000,000. Others suggested that amounts ranging up to the first $100,000 should be exempt from tax. Under all the proposals, the overall effective tax rate would be sharply reduced.

Specific proposals heard at the caucuses include:

	TAXABLE INCOME	TAX RATE
A.	$ 0 - 25,000	17%
	$ 25,000 - 50,000	20%
	$ 50,000 - 75,000	30%
	$ 75,000 - 100,000	40%
	$100,000 - 200,000	42%
	Over $200,000	46%

B.	$ 0 - 25,000	12%
	$ 25,000 - 50,000	15%
	$ 50,000 - 100,000	17%
	$100,000 - 200,000	20%
	$200,000 - 300,000	30%
	$300,000 - 400,000	40%
	$400,000 - 500,000	42%
	Over $500,000	46%
C.	$ 0 - 100,000	10%
	$100,000 - 250,000	15%
	$250,000 - 500,000	20%
	$500,000 - 750,000	30%
	$750,000 - 1,000,000	40%
	Over $1,000,000	46%

Individual Taxes

A reduction in corporate taxation benefits only small business enterprises that are incorporated. It provides no benefits for those organized as sole proprietorships or partnerships, or to those that have made the subchapter S election. Accordingly, there should be a concurrent reduction in the individual tax rates. The present maximum individual tax rate of 70% should be reduced to 50%.

To the extent that distributions from unincorporated entities are considered compensation, the present maximum tax of 50% applies to earned or personal service income. However, when such distributions are deemed to be dividends, the higher 70% tax rate applies. Eliminating the distinction between earned and unearned income by applying the same 50% maximum tax rate to each would aid capital formation by providing an incentive for investment in unincorporated businesses since owners would receive a greater after-tax return on their investments. Perhaps the greater benefit, however, would be the simplicity of tax administration, achieved by applying the same tax rates to compensation and dividend distributions. Costly litigation could be avoided.

Indexing

One compelling reason for making tax rate reduction the conference's number one priority is the erosive impact of inflation. Many critics of our tax system note that persistent inflation has provided a significant windfall to government by taxing inflated dollars at ever higher rates. Voicing this criticism, the delegates noted that various portions of the tax code should be indexed to reflect the continual push of inflation. Although the delegates never indicated that indexing was a top priority item, their overall concern makes it imperative that any discussion of tax policy should take inflation into account. Accordingly, the delegates stated and implied that the brackets should be indexed, and that code sections containing specific dollar amounts (e.g. the $100,000 limitation on used equipment eligible for the investment tax credit, or the $3,000 limitation on tax-free gifts) should be indexed.

As examples of the pressing need for some sort of indexing, two examples can be cited: first, the original $25,000 corporate surtax exemption was placed in the tax code in 1938. If that $25,000 exemption had been increased in relation to purchasing power and according to traditional economic indicators, the examption would now be $125,000. Secondly, in the investment area, research has shown that during the early 1970's, a period of relatively high inflation, the revenues from taxation of capital gains were, in real dollar terms, derived from taxes imposed on an overall net loss.

Moreover, indexing would impose spending discipline on legislators who would recognize that they have less money, in real dollars. For example, in Canada, the rate of increase in government spending has slowed markedly since the tax system was indexed.

Opponents of indexing feel that indexing merely treats the symptoms of inflation rather than attacking its root causes. They believe that indexing the tax code dampens incentives to curb inflation, since inflation's effects are not felt so keenly.

Legislation

Currently, no bill has been introduced which closely reflects this option as written. However, S.1288 and H.R.4140, have been introduced recommending change in the graduated rate scale.

Option 2

Adopt a simplified capital cost recovery system to replace the present complex Asset Depreciation Range (ADR) regulations.

Discussion

Since 1962, depreciable assets have been grouped into classes for purposes of determining useful lives for depreciation purposes. In 1971, an optional depreciation system, known as the Asset Depreciation Range, was adopted. The ADR System grants the taxpayer a 20% range for determining the depreciable life of an asset. For example, a taxpayer having an asset whose class life is five years may depreciate that asset over a life of either four, five or six years. The ADR System, however, has the disadvantage of being extremely complex. Presently, it is used by only a very small portion of the nation's small businesses. Accordingly, a simplified capital cost recovery system is needed.

The great advantage of a simplified depreciation system would be its greater availability to small businesses because of its ease of calculation. Even the Treasury has acknowledged that the present system is burdensome for both the taxpayer and the Internal Revenue Service.

The new proposed capital cost recovery system would replace the ADR system with an entirely new scheme. Under this proposal, assets would be classified into one of three groups, each having a different cost recovery period, thus abandoning the traditional system based on useful lives and salvage value. Class I assets would consist primarily of buildings and structural components. Class II assets would consist primarily of machinery and equipment, and Class III assets would apply to short-lived assets, such as automobiles and light duty trucks. Property would be amortized according to its class. Class I assets would be amortized over 10 years, Class II over 5 years, and Class III over 3 years.

In addition to its simpliciy, a primary advantage of the proposed capital cost recovery system is that a taxpayer could choose to deduct all or a portion of the cost recovery allowance in any given year. Any unused portion of the allowance could be carried forward indefinitely and deducted in future years. This would permit flexibility for companies in loss positions or with widely fluctuating income.

Many delegates - to insure that the benefits would accrue primarily to small business - suggested imposing a limit on the amount of the total depreciation deduction, or on the value of assets to which the 10-5-3 scheme would apply.

Because of the substantial amounts of tax revenues involved in this new approach, the proposed system would be phased in over a period of five years.

See Legislation Appendix, summary of H.R.4646 and S.1435.

Option 3

Reduce the capital gains tax rate according to the length of time an asset is held.

Discussion

In 1978 the maximum tax on a gain from selling a capital asset held for more than one year was reduced from 49% to 28%. Since that date, many business leaders have advocated further reductions in capital gains tax rates.

One way of lowering the capital gains tax is to use a sliding scale measurement. This means that the longer an asset is held, the smaller the taxable portion of the gain would be. Under present law, 60% of the gain on sale of an asset is excluded from taxation. If a sliding scale were in effect, the exclusion would increase for each year an asset was held beyond the initial one year holding period. Under a 2% sliding scale, the exclusion would increase by 2% for each year the asset was held. Thus, if an asset were held for 10 years, 80% of the gain would be excluded from taxation [60% plus (2% times 10 years) = 80%]. This approach has been proposed in bill form in Congress on many occasions, but has not been given active consideration for many years.

The principal advantage of a sliding scale is that it takes into account the artificial gains brought about by inflation. For example, $100 invested in 1947 has a real value of about $30 today. $100 invested in 1967 is worth about half that now. A high capital gains tax coupled with high rates of inflation result in a tax which some view as confiscatory. Recent research has indicated that during this decade's high inflationary period, the tax on so-called gains has, in real dollars, actually been a tax on a net loss.

A second advantage of a sliding scale is that it rewards those who have owned and operated a small business for many years and continually plowed the profits back into the company. A sliding scale allows those individuals who have held their assets for long periods of time to realize a greater return on their capital investment.

The greatest disadvantages to a sliding scale are the complexities and potential inaccuracies in determining when an asset was actually acquired, and then applying a variable formula to determine the amount of gain which should be taxed.

Option 4

Permit deferral of taxes for roll-overs of investments affecting small businesses.

Discussion

Under present law, any gains on sales of business property are taxable in the year in which the transaction occurs. However, there are exceptions in which taxes are deferred, such as the sale of an individual's principal residence, the exchange of investment real estate and depreciable property used in a trade or business, and the exchange of stock and securities in corporate mergers and reorganizations.

Capital formation advocates argue that taxes should be deferred whenever the proceeds from one asset are reinvested or "rolled over" into investment in a small business. Several different plans have been proposed for such roll overs.

The proposal with the broadest application would allow a tax deferral if the proceeds from the sale of any capital asset were reinvested in a small business. This would make more venture capital available for small and innovative businesses.

Delegates were more interested in two other proposals that focus specifically on the continuity of small business ownership.

The first would allow individuals who own an interest in a small business with a networth of $25 million or less to sell their interest for cash and defer any capital gains tax, provided they reinvest the proceeds in a qualified small business within a given time period.

A more narrowly applicable roll-over proposal would solve a serious tax planning problem for retiring individuals who wish to dispose of their businesses. Under this proposal, retiring small business owners could defer taxation if the proceeds from selling their businesses were reinvested in certain qualified assets within time limitations.

Under present law, there are three options available to the seller of a small business. He can sell to an individual, he can sell to another closely-held company, or he can transfer the interest in his business to a publicly-held company in exchange for that company's stock. The first two result in substantial capital gains taxes. Under present law, only the third permits tax deferral - which encourages greater and greater corporate concentration through mergers. If a roll-over tax deferral were adopted, all three transactions would receive equal tax treatment, and a seller would no longer feel compelled to seek a merger.

A disadvantage to each of these proposals, however, is the difficulty in defining what investments would qualify for the roll-over deferral.

See Legislative Appendix, summary of H.R.5097.

Option 5

Provide an effective jobs tax credit for small businesses.

Discussion

In 1977, Congress created a new jobs tax credit. Under its terms, a taxpayer was allowed a tax credit of up to $2,100 for each new employee he hired during the year, up to a total maximum credit of $100,000. However, the jobs credit was amended so that beginning in 1979, the credit would be available only if employers hired members of any of seven target groups. The target groups were designated on the basis of their low income or because, as a matter of policy, their employment should be encouraged. The targeted credit is available for the first and second year of a worker's employment. A return to the general jobs credit approach would be of great utility to the small business community.

The primary benefit of a jobs credit is that it provides a benefit to businesses which are labor intensive rather than capital intensive. Small businesses do not generally receive the full benefits of the investment tax credit, since, as a rule, they are more labor intensive than large companies. Numerous studies have concluded that the greatest job growth in the economy is in the small-to medium-sized sector rather than in the large industrial sector. Delegates emphasized that in many cases the jobs tax credit determines whether or not they can add employees.

The primary disadvantage of both the general jobs credit and targeted jobs tax credit is the difficulty of computation. The credit is based on the employers' wage base under the Federal Unemployment Tax Act, and contains several threshold tests which the taxpayer must meet. In addition, several limitations were placed on the credit, thus limiting its general applicability. The targeted approach, while it does attempt to provide employment for disadvantaged and/or unskilled workers, has two major drawbacks. First, it does not provide relief for areas of the country which experience extremely high unemployment rates. Second, it is not generally available to all firms, simply because very few members of the targeted groups reside in certain areas of the country. These difficulties could be eliminated by either returning to the general jobs credit approach, or by adopting a two-tiered tax credit, with one tier being a general jobs credit, and a second, perhaps more generous, credit being available for targeted groups. Delegates gave wide support to the two-tier approach.

Option 6*

Eliminate double taxation of dividends.

Discussion

Under present law, corporations pay taxes on profits, then distribute all or part of those profits to shareholders in the form of dividends; the shareholders then pay personal income tax on the dividends. Many plans have been proposed to eliminate this double taxation, but corporations and shareholders have never been able to agree on who should benefit, the corporations or individuals.

Delegates made several suggestions to eliminate from corporate taxation the tax on dividends paid. Some suggested a special provision available only to small businesses of a deduction of up to $500,000 for dividends paid. Others advocated a deduction for all dividends paid by all corporations, with no dollar limitation. The middle ground was a graduated deduction scale, with various increments having been proposed. A similar approach would allow a tax credit for dividends paid.

Suggestions for eliminating double taxation at the shareholder level took the form of providing additional investment incentives. The most direct approach is simply to amend the present $100 exclusion to provide a $1,000 exclusion. Another relatively simple change would be to change the treatment of dividends for the purposes of the maximum tax to allow dividends to be treated as earned, rather than unearned income. Thus, the maximum tax rate on dividends would be 50% rather than 70%. Tax simplification could be achieved in some measure by eliminating the accumulated earnings tax, as discussed elsewhere in this document. Finally, a tax deferral system could be implemented, under which any dividends reinvested within a certain time period in designated assets, would escape taxation until a final distribution.

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* New option proposed at Regional Delegate Caucus.

Option 7

Provide tax incentives in the form of a new security called a Small Business Participating Debenture (SBPD) to provide a source of capital for small businesses.

Discussion

Small businesses have a substantial need for capital beyond that which can be generated by the business itself, and yet they are often not attractive investments for investors. Many entrepreneurs are not interested in relinquishing a portion of their equity in their business for additional capital if it can be avoided. The price is simply too high. Furthermore, a minority interest in a small business is not an attractive investment even when available because it lacks liquidity and is not easily marketable.

A new form of security could provide needed capital.

The SBPD would be a debenture, but the lender would receive a stated rate of interest and a share of the earnings of the business during the period that the debenture is outstanding. The investor would be permitted to share in the fortunes of the business in much the same way as a traditional stockholder, but participation would terminate when the debenture is paid off rather than continuing indefinitely.

Legislation has been introduced in the current session of Congress which would create certain tax incentives, including capital gains treatment to the lender on the share of earning payments and a tax credit for investing in an SBPD. The small business would be entitled to view both the interest and the share of earnings payouts as a cost of capital and deduct both of them as ordinary interest.

No corresponding instrument exists currently in the marketplace, and thus, the effectiveness of the SBPD in attracting additional capital remains speculative at this point in time. However, many businessmen, bankers, etc., who have been exposed to the idea have indicated that it should provide a significant incentive to bring debt capital into small business on terms which are attractive to an investor and acceptable to the typical borrower.

Option 8

Increase to $500,000 the allowable earnings accumulation before the imposition of an accumulated earnings tax.

Discussion

Small businesses often have limited access to bank lending (or find themselves having used all of the bank lending that is available) and, as a practical matter, they are not candidates for the equity markets. Accordingly, small businesses tend to reinvest earnings in their operations each year, yet often find revenue agents accusing them of accumulating income beyond the reasonable needs of the business. The accumulated earnings tax is a very small revenue gainer for the Treasury, since many cases are fought successfully by the taxpayer. However, litigation is time consuming and expensive.

If the Treasury Department feels that the accumulated earnings must remain on the books to prevent abuse situations, there should at least be an adjustment of the amount which may be accumulated. The minimum allowable accumulation has stood at $100,000 for many years, but is insignificant in relation to the capital needs of small business and the effect of inflation on this arbitrary dollar limitation. Delegates favored raising the allowable accumulation to $500,000, or eliminating the accumulated earnings tax altogether.

Option 9

Permit capital expenditures to be expensed immediately rather than depreciated or amortized over a term of years.

Discussion

Under this proposal, the cost of a capital expenditure would be deducted in the year an asset is purchased or placed in service, rather than depreciated over a term of years. This approach would provide companies with a great incentive to improve their productive assets because their cost could be deducted immediately.

Proponents of this approach cite the tremendous productivity increases that would result as the nation's industrial plant was modernized. Since the U.S. trails the eight leading industrial nations in productivity, this enhancement of our domestic production capacity would produce a significant benefit to the competitiveness of United States industries abroad. In addition, jobs would be created, and trade deficits potentially lowered.

The primary disadvantage to this approach is its enormous cost to the U.S. Treasury. No doubt a lengthy phase-in period would be required. The phase-in could be structured with either an annual dollar amount limitation or a percentage limitation, under which deductions would be allowed up to a certain percentage of income or percentage of capital expenditure.

Many delegates believed that if this approacn was not feasible for all capital expenditures, it should at least apply to government mandated expenditures.

Option 10

Provide tax credits for direct investment in small businesses.

Discussion

Under present law, there is no direct tax incentive for investing in small businesses. In fact, disincentives exist. Small businessmen wish to avoid the burdens of registration with the SEC, and investors find that it is often difficult to liquidate equities in small companies at a fair price. Accordingly, legislation has been introduced to give an individual tax investor a tax credit of up to $750 (10% of the first $7500) for investing in qualified new stock issues during a taxable year.

The greatest advantage of this plan is that it would provide a direct incentive for investment in small businesses. Investors must be protected from "fly-by-night" corporations but, overall, a credit would provide a new source of equity financing for the nation's small, innovative companies. Since many small companies must go to foreign sources for their capital, this proposal would make domestic equity markets more readily accessible to small businesses.

The primary disadvantage of the proposal is that many believe it would provide no true incentive. Recently, individual investors have been steadily withdrawing from traditional capital markets. Since 1974, there has been only a handful of offerings in companies with less than $5 million in assets. Opponents of the proposal argue that since there are so few offerings into which investors could channel their funds, this bill would provide no true incentive. However, more recent indicators show an upswing in the number of offerings, attributed by some to the incentives of the reduction in capital gains taxes, and seeming to indicate that tax incentives do promote investment.

S.487 and S.655 have been introduced to provide this tax credit.

Option 11*

Revise estate tax laws to ease the tax burden on family-owned businesses, and encourage the continuity of family ownership.

Discussion

People who inherit a small business often find themselves in the difficult position of needing to liquidate the enterprise in order to pay the estate taxes. This frequently results both in the loss of small business and, when the heirs sell out to another company, in greater business concentration.

To address this problem, the delegates suggested two revisions in how an estate is valued. The first suggestion proposed that the initial $500,000 in the value of an estate be either exempt from taxation or deducted from the total value of the estate.

The second proposal was an extension of the present marital-deduction concept, under which a surviving spouse is allowed a deduction from the estate of $250,000 or 50% of the value of the adjusted gross estate, whichever is greater. Delegates proposed extending this concept to include other family members who are shareholders of a closely-held business.

A third proposal would revise a provision in the 1976 Tax Reform Act that permits extended payout of estate taxes for certain closely-held businesses. Under the provision's current terms, heirs may defer the first payment of estate taxes up to five years following the death of the descendant; thereafter the tax can be paid in ten equal annual installments. Moreover, a special low interest rate of 4% applies to the first $1,000,000 of closely-held business property.

To qualify for this special provision, however, the closely-held business must comprise more than 65% of the adjusted gross estate. Many delegates believed that this 65% threshold should be lowered significantly. In addition, some felt that the special 4% interest provision should not have a dollar limitation.

Option 12

Improve inventory pricing regulations by simplifying the LIFO inventory system for small businesses and permitting small business with inventories below $100,000 to use the cash method of accounting.

Discussion

As is true of business in general, small businesses suffer from inflation. One result of this is that they generally find themselves paying taxes on so-called "inventory profits." The LIFO method of accounting for inventories permits elimination from income of the higher cost of replacement inventories. However, the LIFO regulations are extremely complex, and as a practical matter, the small businessman often foregoes the use of this method because of this complexity.

A simplified LIFO system could be adopted so that inventory records can be maintained on a first-in first-out basis. LIFO results can then be obtained by simply applying government published indices to the inventory. Only a few simple computations would be required to determine the reportable amount of inventory.

The current LIFO inventory regulations require that inventory records be maintained in "layers" and decreases in inventory result in adjustments of layers in the reverse order they were accumulated. In order to maintain a simplified approach, it is further recommended that the LIFO inventory computed on an index method be maintained without regard to layering and that the adjustment required in the event of a decrease be based upon the average LIFO cost in inventory at the beginning of the year.

Small businesses are not unlike others in having to pay taxes currently while funds are tied up in inventory and receivables. However, small businesses, and particularly the smallest of these, have the least access to external sources of capital and are hardest pressed by this requirement. It is suggested, therefore, that companies with less than $100,000 in inventory be permitted to use the cash method of accounting, recognizing neither receivables nor payables in the determination of income, and charging inventory to expense as it is purchased.

Option 13

Provide an investment tax credit available for all investments in qualified depreciable business assets, without making a distinction between new and used property.

Discussion

Under present law, an investment credit of 10% of cost is allowed for investments in qualified depreciable business assets. The credit in any one year cannot exceed the first $25,000 of tax liability, plus 60% of tax liability in excess of $25,000. (The 60% figure will increase to 70% in 1980, 80% in 1981, and 90% for 1982 and subsequent tax years). A limit of $100,000 ($10,000 tax credit), is imposed on investment in used property eligible for the credit.

Eliminating the distinction between new and used property would allow companies with limited capital resources to secure the greatest benefit for plant enhancement, because no limitation would be imposed on the kind of property to which the credit would apply. Even if companies cannot afford the newest, most modern equipment, they should be allowed to receive the maximum tax benefit from any improvements in plant capacity and productivity that can be achieved, either from new or from used property.

Opponents of eliminating the distinction point out the purpose of the investment tax credit was to provide companies an incentive to invest in the newest, most productive asset, not the marginally effective technology of displaced equipment.

Option 14*

Congress should enact legislation to equalize the treatment of fringe benefits and retirement benefits for large and small entities.

Discussion

For many years, the Internal Revenue Service, Congress, and taxpayers have fought bitter battles over the treatment of fringe benefits, to the extent that Congress has imposed a moratorium on any changes in regulations on fringe benefits through June, 1981. However, even under present law, there are certain inequities between large and small businesses entities which sometimes unduly inhibit the smaller entities from providing attractive benefit packages to their employees.

The most glaring deficiency is in the area of retirement benefits. Many small business are hard pressed to provide adequate retirement benefits. Under present law, participants in a qualified pension or profit sharing plan may not receive tax benefits for participation in Keogh plans or individual retirement accounts even though their employers' plans might not be adequate. The availability of these two mechanisms should be extended to the owners and employees of small businesses without regard to participation in qualified plans.

A second problem in the benefits area relates to the cost of benefits other than retirement plans. The costs of employee benefits are often prohibitive to small business owners and operators. Thus, employees and even owners of small businesses often do not have adequate benefits available to maintain an incentive to stay in the business.

One way to equalize the tax advantage enjoyed by larger entities would be to change the method of tax calculations, and thus provide more funds for benefits for small businesses. Under this proposal, corporate taxes would be calculated before the deduction of retirement costs, medical insurance costs, life insurance costs, legal benefits costs, and other employee benefits, etc. Then, the cost of these employee benefits would be totaled, and that total multiplied by the applicable corporate rate, and deducted from the previously calculated corporate tax. Smaller entities would then receive a proportionately larger tax benefit for the expenses of their employee benefits.

Option 15*

Provide a 90% SBA guarantee for small business industrial revenue bonds.

Discussion

Small business generally have been excluded from a very important source of capital formation - the Industrial Revenue Bond. This program has been in effect for several years, and expanded with the Tax Reduction Act of 1978. Due to the unmarketability of small company's bonds, however, small business has not participated in this program.

Large corporations use the IRB program to build plants and purchase equipment. The benefit to this financing is that these businesses are able to borrow funds at rates 2 to 4 points below prime.

To provide this opportunity for small businesses, the bonds of a small company need to be more marketable. This could be accomplished through SBA 90% guaranteeing the bonds. In making the bonds marketable, it would allow small buisnesses to avail themselves of a program that increases the supply of capital, at attractive interest rates

The SBA has successfully implemented, on a test basis, an IRB program in conjunction with EPA requirements. As both the IRB and guaranteed bond approaches are tested, long periods of legislation evaluation would not be required.

See Legislative Appendix, summary of H.R.2460.

OTHER OPTIONS

In revising the Option Papers, there were other significant options, both from the original draft and new ones proposed at the Regional Delegate Caucus, which delegates may want to consider further. These options, without commentary, are listed below.

Option 16

Repeal the carryover basis provisions of the 1976 Tax Reform Act.

Option 17

Amend the Investment Advisers Act and the Investment Company Act of 1940 or Permit Public Ownership of Venture Capital Companies.

Option 18

Clarify the "Prudent Man Rule" to insure that securities of small issuers are not excluded from those securities eligible for purchase by funds subject to ERISA.

Option 19

Reinstate the qualified stock option, deferring the tax on the gain, in stock received by employees of small business, until the stock is sold.

Option 20

Establish a separate class of investors, certified by the SEC, to whom small, registered companies, would not have to make full disclosure.

Option 21

Permit secondary market pooling of commercial bank guaranteed small business loans.

Option 22*

Using the model of savings and loans and their importance to real estate loans, develop an infrastructure of Business Development Banks to attract depositors and investors for the primary purpose of making loans to small business.

Option 23

Repeal time limits on the use of carryovers on net operating losses and capital losses.

Option 24

Revise Subchapter S to: expand the number of shareholders permitted; to eliminate restrictions on those persons who can be shareholders; and to allow the allocation of specific items of income, expense credit, etc. to shareholders in a manner similar to partnerships.

Option 25

Increase the amount of income tax triggering the requirement to make estimated tax payments to $1,000.

The Conference wishes to express great appreciation to the following members of the Task Force on Capital Formation and Retention, who gave unsparingly of their time and resources to this project.

Chair:	Edgar F. Heizer, Jr. Chicago, Illinois
Commissioner:	Sheldon Lubar Milwaukee, Wisconsin
Members:	Richard Cummings Philadelphia, Pennsylvania
	Marvin Dickman Chicago, Illinois
	William R. Hambrecht San Francisco, California
	Garnet Keith Newark, New Jersey
	Bruce A. Mann San Francisco, California
	Gerald Mehlam Beverly Hills, California
	Edward H. Pendergast Boston, Massachusetts
	Marion Sandler Oakland, California
	Dean Treptow Brown Deer, Wisconsin
	John S. Wadsworth New York, New York
Professional Staff:	James V. Manning Atlanta, Georgia
	Don M. Currin Atlanta, Georgia

OPTIONS	CHAMBER POSITION
13. Increase the amount of income tax triggering the requirement to make estimated tax payments.	*Under study.*
14. Make an investment tax credit available for all investments in qualified depreciable business assets, without making a distinction between new and used property.	*Chamber supports increase in limits to $200,000.*
15. Repeal the carryover basis provisions of the 1976 Tax Reform Act.	*Chamber supports. Action needs to be taken on this before December 31, 1979.*
18. Increase the number of "Class C" directors who serve on the Boards of Federal Reserve Banks.	*Chamber supports.*
20. Amend Treasury Regulation T to permit installment sales of certain limited partnership interests.	*Needs further study.*
21. Clarify the "Prudent Man Rule" to insure that securities of small issuers are not excluded from those securities eligible for purchase by funds subject to ERISA.	*Moot point, has already been done.*
22. Establish an investment tax credit for employer contributions to employee stock ownership plans (ESOP) and revise the formula for calculating tax for employees who exercise this option.	*Under study.*
23. Establish a separate class of investors, certified by the SEC, to whom small, registered companies, would not have to make full disclosure.	*Needs further study.*
Chamber would add:	
24. Amend Section 12G of the Securities Act of 1934 to raise the level at which all corporate reporting is required to $5,000,000 and 2,000 stockholders; in the future, coordinate this level with the limits contained in SEC Regulation A pertaining to initial offerings.	*Chamber supports.*

OMNIBUS SMALL BUSINESS CAPITAL FORMATION ACT OF 1981
(As amended and adopted by the Board of Directors
of the Yuma County Chamber of Commerce on March 26, 1981)

The provisions of the Omnibus Small Business Capital Formation Act of 1981 fall into five broad categories:

1. Capital Formation -- to improve the ability of small business to attract needed capital from external sources of financing by providing greater incentives for investors.

   A. Investment tax credit for investments in new stock issues of small businesses. A ten percent tax credit (up to $1,000 per person) would be provided for an investment in stock issued by business *with less than one million dollars in taxable income, and limited to those corporations not required to file with the Securities Exchange Commission.*

   B. Authorize the creation of a new financing instrument, the "Small Business Participating Debenture" (SBPD). The SBPD would be a hybrid security, with elements of equity and debt capital. SBPD's issued by eligible firms *with less than one million dollars in taxable income, and limited to those corporations not required to file with the Securities Exchange Commission* would bear a relatively low stated rate of interest, but also could involve a distribution of the company's earnings, which would be taxable to the investor at the preferential long term capital gains rate.

   C. Capital gains tax reduction for individuals and corporations, with maximum rates reduced from 28 percent to 20 percent.

   D. Capital gains "rollover." Gains resulting from the sale of an investment in a small business would not be recognized if reinvested in another qualifying small business within 18 months.

   E. An increase in the maximum number of shareholders permissible for Subchapter S corporation election from 15 to 100. This would improve the access of small businesses to new sources of capital.

   F. Broker-dealer Reserve. Would permit dealers "making a market" in a small business equities to transfer, with deferred tax recognition, up to an aggregate of $1 million capital gains resulting from the sale of such stock, to reserve for future marketing-making activities. This would greatly enhance the marketability of small business stock.

II. Capital Retention -- to permit small businesses to retain a greater share of internally generated capital.

   A. Graduation and reduction of corporate tax rates. Would increase the number of brackets to seven and reduce tax rates, particularly helpful for smaller businesses. Present law corporate tax brackets and rates are as follows:

Taxable Income	Tax Rate (Percent)
$0 to $25,000	17
$25,000 to $50,000	20
$50,000 to $75,000	30
$75,000 to $100,000	40
$Over $100,000	46

Under the bill, brackets, and rates would be:

Taxable Income	Tax Rate (Percent)
$0 to $25,000	15
$25,000 to $50,000	17
$50,000 to $75,000	25
$75,000 to $100,000	30
$100,000 to $150,000	35
$150,000 to $200,000	40
Over $200,000	44

B. Accelerated and simplified depreciation tax treatment for more realistic capital cost recovery for smaller businesses. Bill would propose "5-3" classification (from 10-5-3) for equipment and vehicles, respectively, with ten percent investment tax credit for 5-year class investments and 6 percent credit for investment in trucks and other vehicles. First $100,000 of small business investment not subject to any phase-in period. Bill would not address question of depreciation for structures.

C. Increase in the amount of permissible accumulated earnings from $150,000 to $300,000. Accumulated earnings tax would apply only to amounts in excess of $300,000.

D. Increase in the ceiling on the used property investment tax credit from $100,000 to $250,000.

III. Estate Tax Reforms -- to reduce onerous burden of gift and estate taxes on small businesses.

A. Increase the present estate tax exemption from $175,000 to $600,000.

B. Provide an unlimited gift and estate tax.

C. Increase the annual gift tax exclusion from the current limit of $3,000 to $5,000 per year per donee.

D. Make several changes in special use valuation rules for farmland and closely held businesses. *(Would like to see clarification.)*

E. Set the value of gifts made within three years of decedent's death at the value at the time of the gift rather than at the date of death.

F. Permit the 5-year deferral / 10-year installment election for payment of estate taxes, provided that at least 35 percent of the gross estate or 50 percent of the taxable estate is a closely held business. (Present law limitation is 65 percent of adjusted gross estate.)

G. *Permit partial-sale of property under tax lien for pro-rata payment on such sale*

IV. Employee Stock Options -- bill would permit employees to exercise stock options without tax consequences, as opposed to present law requirement of paying ordinary income tax on "spread" between option price and market price. Employees would be eligible for capital gains treatment when the stock is sold, with option price being cost basis. This provision would enable smaller businesses to attract better management by encouraging the use of stock options for key employees. Bill would include conditions set forth in H.R. 5829 as reported by Senate Finance Committee in 1980.

V. Inventory Accounting for Small Business -- inflation has effect of creating illusory profits for firms on "first in - first out" (FIFO) inventory accounting, since reported "cost of goods sold" are based on original, lower inventory prices as opposed to more recent, inflated inventory prices. Lower "cost of goods sold" means higher taxable incomes and tax liabilities. Conversion to more realistic "last in - first out" (LIFO) method is very complicated and costly for smaller business. Under the bill:

A. Cash accounting (immediate expensing) would be permitted for businesses with total annual sales of $1 million or less.

B. Tax penalty associated with conversion to LIFO, which results from requirement to take back into income all previously written down inventories, would be payable over ten-year period.

C. Bill would delay until after December 31, 1980, compliance with Revenue Procedure 80-5 and Revenue Ruling 80-60, which require taxpayers to take back into income the value of erroneously written down inventories (Thor Power Tool Case), to give small business more time to comply.

1. *Eliminate double taxation by making the first $250,00 in dividends tax deductible to the corporation.*

2. *Grant ten percent investment type tax credits on interest expense on the first $100,000 of interest per year.*

NOTE: Chamber of Commerce amendments *italicized*

SMALL BUSINESS ADMINISTRATION

13 CFR Part 120

Business Loan Policy; Advance Notice of Proposed Rulemaking

AGENCY: Small Business Administration.

ACTION: Advance notice of proposed rulemaking.

SUMMARY: The SBA proposes, due to the adverse impact of escalating interest rates, to make four changes in its interest rate policy regarding variable rate guaranteed loans. The changes, if adopted, would apply to loans approved on or after October 1, 1981. The proposed changes are that (1) Participating lenders would be permitted to use their own prime rate as a base for computing interest rate fluctuations, subject to certain conditions, (2) variations in the note rate could fluctuate as frequently as daily, (3) participating lenders would no longer be required to notify SBA of changes in the note rate and (4) the SBA optional peg rate would no longer be an acceptable base for computing interest rate fluctuations.

DATE: Comments must be received on or before August 13, 1981.

ADDRESSES: Written comments, in duplicate, may be sent to the Director, Office of Business Loans, Small Business Administration, 1441 L Street, N.W., Washington, D.C. 20416.

FOR FURTHER INFORMATION CONTACT: Questions about this advance notice can be directed to: Richard L. Wray, Financial Analyst (202) 653-6470.

SUPPLEMENTARY INFORMATION: The adverse impact escalating interest rates are having on small businesses has become increasingly apparent over the past months. The present SBA interest rate policy was examined in order to identify steps the Agency could take to relieve the impact. Four proposed actions have been identified.

SBA is hereby providing the public an opportunity to review these proposals and comment on them.

SBA is proposing that its participating lenders would be permitted to use their own "prime" as a base in computing interest rate fluctuations provided (1) the appropriate regional administrator has authorized the lender to use its own prime, (2) the lender's prime is printed daily in a news publication of general circulation within the lender's service area, (3) the "initial" note rate does not exceed SBA's maximum acceptable rate, (4) the spread (plus or minus) between the lender's prime and the initial note rate is maintained during the life of the loan and (5) regional administrators may withdraw the authorization for the lender to use its own prime as a base because the lender no longer meets the conditions, the lender has abused the authority or other similar cause. The meaning of the fourth condition is best explained with examples. Assume an initial note rate at SBA's maximum acceptable rate at 20 percent and a lender's prime at 18 percent. The note rate is 2 percent over the lender's prime and this 2 percent spread over the lender's prime must be maintained during the life of the loan. Before a regional administrator can authorize a lender's use of its own prime the regional administrator must have evidence that the rate is actually published daily. The fact that a lender sends periodic press releases to newspapers announcing its prime rate does not satisfy this requirement unless the rate is actually published each business day.

Many lenders have said that the additional administrative costs caused by SBA policies force a higher interest rate on SBA loans. The primary policy cited as the cause of increased cost is the fluctuation period. Lenders normally adjust the fluctuating rate on non-SBA loans daily. SBA loan quarterly interest rate adjustments must, therefore, be posted "off line" at greater expense. The change to daily adjustments on SBA loans eliminates this extra expense. The initial fluctuation cannot occur until one day after the note is signed and the loan closed, regardless of when disbursed. This allows the SBA to establish an initial interest rate, using the selected base published the day SBA received the application. Many lenders "close" a loan before any funds are disbursed to permit filing of lien positions. Even if funds are disbursed at closing, the lender can adjust the rate the next day with no more than one day's interest loss to either party to the loan.

Presently participants are required to notify SBA of every change in the note interest rate. Because SBA no longer needs to monitor these changes and because SBA's resources are not adequate to monitor daily changes, this requirement would be eliminated. This is the only proposed change that would apply to existing loans and new loans.

The SBA Optional Peg Rate was established as an alternate base to the money center prime. Lenders seldom use this base and it would not be possible for SBA to compute and publish this rate in a timely manner on a daily basis. Therefore, the use of the optional peg rate would not be permitted for new loans. SBA would continue to publish this rate each quarter as long as any loans that use this base to compute fluctuations are still outstanding.

This advance notice of proposed rulemaking will afford the public 15 days to comment on SBA's intentions. At the close of that comment period, SBA will review the comments and incorporate them into a proposed rule which will then be published. The public will have 30 days to comment on the SBA proposed rule. The present proposal is as follows:

Section 120.3(b)(2)(iii)(B) is revised and a new § 120.3(b)(2)(iii)(C) is added to read as follows:

§ 120.3 Terms and conditions of business loans and guarantee.

* * * * *

(b) * * *

(2) * * *

(iii) * * *

(B) Subject to paragraph (b)(2)(iv) of this section, and for loans approved on or after December 1, 1979, and before October 1, 1981, a participating lender may utilize a fluctuating rate of interest. The fluctuations may occur not more than quarterly, and must rise and fall on the same basis. Fluctuation periods commence on the first day of a calendar quarter (e.g., Jan. 1, April 1, July 1, Oct. 1). The initial interest rate on the loan shall not exceed SBA's maximum acceptable rate as of the date the loan application was submitted by the lender to SBA, and the initial rate must remain in effect for not less than one full fluctuating period (e.g. one full calendar quarter) after first disbursement. Thereafter, the publication of, or variations in SBA's maximum acceptable rate shall have no further effect or application when the interest rate on the note fluctuates as the base rate fluctuates. The base rate for fluctuating interest may be either the prime rate in effect on the first day of the fluctuation period and published daily in a public print media, or the SBA Optional Peg Rate which is published in the Federal Register quarterly by SBA. For loans with maturities under seven (7) years, the increase in interest to be added to the base rate may be established by the lender up to, but cannot exceed, two and one-quarter (2¼) percentage points. For loans with maturities of seven (7) or more years, the increase in interest to be added to the base rate may be established by the lender up to, but not to exceed, two and three quarter (2¾) percentage points, without regard to SBA's maximum acceptable rate as provided in this paragraph. Amortization of the loan may be either by fixed principal amounts plus interest at the specified rate for the particular fluctuating period, or by equal payments combining principal and interest: *Provided, however*, that the equal payment may be based on an interest rate higher than the note rate to insure that future payments will be sufficient to pay interest on the outstanding principal.

(C) For loans approved on or after October 1, 1981, a participating lender may utilize a fluctuating rate of interest. The fluctuations may occur no more frequently than daily and must rise and fall on the same basis. Fluctuation periods may commence the day after a borrower signs the note and the loan is closed, regardless of when disbursed. The initial note rate shall not exceed SBA's maximum acceptable rate (pursuant to paragraph (2)(iv) of this subsection) as of the date the loan application was received by SBA. The base rate may be either the minimum money center prime rate published daily in the *Wall Street Journal* or, when authorized by the appropriate regional administrator, the lender's prime rate. Regional administrators may authorize a lender to use its own prime as a base whenever the lender's prime rate is published daily in a news publication of general circulation in the lender's service area and when such lender agrees that the initial note rate will never exceed SBA's maximum acceptable rate and that the spread between the lender's prime and the initial note rate will be maintained during the life of the loan. Regional administrators must have evidence, acceptable to that official, that the lender's prime is published daily and regional administrators may withdraw their authorizations if the lender's prime is no longer published daily, if the lender fails to conform to the conditions of the authorization or for other cause. Amortization of the loan may be either by fixed principal amounts plus interest at a specified rate or by equal payments combining principal and interest: *Provided, however*, that the equal payment may be based on an interest rate higher than the initial note rate to insure that future payments will be sufficient to pay interest on the outstanding principal.

* * * * *

Dated: July 23, 1981.

Michael Cardenas,

Administrator.

[FR Doc. 81-22093 Filed 7-28-81; 8:45 am]

BILLING CODE 8025-01-M

SMALL BUSINESS ADMINISTRATION

Business Loan Policy; Intent To Publish Maximum Acceptable Rate

AGENCY: Small Business Administration.

ACTION: Notice of intent.

SUMMARY: Subsection 120.3(b)(2)(iv) of 13 CFR 120 provides that SBA may, from time to time, publish in the Federal Register notice of the maximum acceptable rate that lenders may charge for SBA guaranteed loans and on the lenders' share of immediate participation loans. The last notice published July 2, 1980, (45 FR 45048) limited the maximum acceptable rate for guarantee loans to the minimum money center prime rate that was printed in the *Wall Street Journal* that was published on the day the SBA received the application plus not to exceed 2¼ percent for loans having maturity under seven (7) years or not to exceed 2¾ percent for loans with maturities of seven (7) or more years. The rate on a lender's share of immediate participation loans is limited to 1 percent below the guarantee rate for a loan with a comparable maturity.

SBA proposes to publish a notice on or about October 1, 1981, that would limit the maximum acceptable interest rate to the minimum money center prime rate printed in the *Wall Street Journal* published on the date SBA received the application. The proposal would eliminate the points that could be added to the base rate. The rate on the lenders' share of immediate participations would be limited to 1 percent below the guarantee rate.

DATE: Comments on this proposed notice must be received on or before August 28, 1981.

ADDRESSES: Comments, in duplicate, may be addressed to the Director, Office of Business Loans, Small Business Administration, 1441 L Street, N.W., Washington, D.C. 20416.

FOR ADDITONAL INFORMATION: Questions about this notice of intent may be directed to: Richard L. Wray, Financial Analyst, (202) 653-6470.

SUPPLEMENTARY INFORMATION: The present SBA allowable rates are based on the "prime" rate actually being the lowest rate banks charge their best customers. The additional percentage points may be added because the SBA guarantee does not make the loan equal to the quality of a bank's loan to its best customer. Recent indications that the best customers are charged rates below the bank's prime make it necessary for SBA to reconsider its maximum acceptable rates.

SBA has considered using such rates as the Federal Funds Rate, the Discount Rate or the Call Money Rate as the base for establishing the maximum acceptable interest rate. These rates are all readily available on a daily basis in a public print media. However, the public is requested to submit suggestions on other rates that could be used as a base for this calculation, or justification for using one of the rates considered.

Dated: July 23, 1981.

Michael Cardenas,

Administrator.

[FR Doc. 81-22094 Filed 7-28-81; 8:45 am]

BILLING CODE 8025-01-M

[From the Congressional Record, July 8, 1981]

THE EFFECTS OF HIGH INTEREST RATES ON SMALL BUSINESS

Mr. BOREN. Mr. President, when money and credit tighten and interest rates rise, small businesses, public utilities and consumers of all types are seriously affected. For small businesses, many of which operate with small profit margins, increases in the cost of borrowing money can cut so heavily into profits that they can no longer afford to borrow money. When the supply of money and credit is limited, the credit rationing that follows discriminates heavily against small businesses.

It is important that the Congress understands that small business accounts for more than half of all the private sector jobs in this country. The public has seen statistics showing that new and small firms—of 100 employees or less—account for about three-quarters of all the new jobs in the economy, 48 percent of the gross domestic product and 43 percent of the gross national product. As bankers tighten up credit and screen borrowers more carefully, the small businessman finds it difficult to borrow at all even if he is willing to pay the 20 percent interest rate.

Personal bankruptcies rose to a record 397,958 in 1980, a 72-percent jump over 1979; almost as many white collar individuals go bankrupt as blue collar workers and 37 percent earn more than $15,000 per year.

Some 48 percent have some college or a college degree and the greatest number are in the 25 to 34 age bracket. The collapse in the number of business loans caused the increase of new bank loans for all purposes to fall from 101.2 billion in 1979 to 34.1 billion in 1980. Small businesses in every sector of the economy are failing from this strict credit availability. In 1980, corporate after-tax profits pegged at $189.9 billion were estimated to be 3.5 percent less than their level of $196.8 billion in 1979. But at $43.3 billion, the inventory valuation for 1980 was the largest for any year ever, and so was the depreciation allowance at $18.1 billion.

Adjusting for these facts, corporate after-tax profits were down 7 percent from their 1979 levels. Furthermore, when inflation is taken into account—the GNP deflator was at least 9 percent in 1980—corporate after-tax profits had dropped 16 percent from the 1979 levels.

We are constantly reminded that small business keeps alive the American dream—that a person can control his own destiny—that he or she can prosper by their own efforts. The well-being and the success of American small business has great implications and therefore it is imperative that these businesses have a chance to operate and produce. High interest rates jeopardize these efforts to produce and accordingly high interest rates must be brought under control.

SMALL BUSINESS PARTICIPATING DEBENTURES

(Mr. ECKART asked and was given permission to address the House for 1 minute and to revise and extend his remarks.)

Mr. ECKART. Mr. Speaker, for many years, Congress has considered various forms of relief for our Nation's small businesses. Unfortunately, these efforts have met with mixed success—the small businessman of today is still struggling under the burden of high interest rates and a lack of access to capital.

I recently introduced legislation that will go a long way in addressing the small businessman's need for capital. It provides for the creation of a new financial instrument called a small business participating debenture, or SBPD.

The small business participating debenture was among the proposals recommended by last year's White House Conference on Small Business. In addition, the SBPD concept has been endorsed by the National Small Business Association, the National Association of Small Business Investment Cos., and many other small business organizations.

The SBPD is a hybrid security, that is to say, it is a cross between a stock and a bond. It is a fixed-term debt instrument structured to carry both a nominal interest rate and a percentage of profit to the investor. The issuing company pays a premium for the use of capital for a limited period of time, in contrast to giving equity rights that allow the investor to participate in a company's earnings long after the borrowed funds have been repaid. The specific terms of the SBPD, such as interest rate, maturity date, and share of earnings would be determined by the market for the security.

Mr. Speaker, it is the tax treatment accorded SBPD's which will make them particularly attractive to investors and small businessmen alike. The interest and profit payments made by the issuing firm would both be fully deductible. On the investor side, the interest would be taxable at ordinary rates, but the profit portion would be taxed at the more favorable long-term capital gain rate.

Certain limitations are embodied in this legislation to insure that the benefits would go to the companies most seriously affected by the capital formation problem—small- to medium-sized companies who may need loans too small for venture capitalists to make. Pursuant to this legislation, a SBPD can only be issued by a domestic trade or business, whether or not incorporated, which has a net equity of less than $10 million. Additionally, no company can have more than $1 million in SBPD's outstanding at one time.

Mr. Speaker, as I stated earlier, the small business participating debenture is a concept that has achieved considerable visability in small business circles. It recognizes the fact that an infusion of new equity into a small business is not necessarily the answer to the capital needs of a business, and it provides an alternative form of financing.

As we all know, a strong vigorous small businessman is important to our Nation. The passage of this legislation would be a big first step toward real economic growth for our small businesses, and a strengthening of the backbone of our national economy. Therefore, I strongly urge my colleagues to join me in cosponsoring H.R. 4015.

ENTERPRISE ZONES: AN ANSWER TO URBAN PROBLEMS

Mr. MICHEL. Mr. Speaker, for the past 20 years or so, we have tried to deal with urban problems through massive Federal Government programs designed to alleviate existing problems. Given the amount of money involved, there were some cases in which temporary easing of specific problems occurred. But this kind of approach tried to treat the symptoms, not the disease of urban blight. What we need is an approach that gets to the heart of the matter. Instead of applying band-aids we have to get rid of the major causes of urban problems: unemployment, underinvestment, and overregulation that discourage would-be businessmen from creating new employment opportunities.

The enterprise-zone concept is a way of dealing directly with all these problems. A recent issue of Constructor magazine gives a view of this idea from the vantage point of the construction industry. It is worth reading.

At this time I wish to insert in the RECORD, "Enterprise Zones" from Constructor, June 1981.

[From Constructor, June 1981]

"ENTERPRISE ZONES

A promising market for municipal-utilities contractors may be indirectly created with the passage of the Urban Jobs and Enterprise Zones Act.

The bill, sponsored by Representatives Jack Kemp [R-N.Y.] and Robert Garcia [D-N.Y.], was introduced to Congress earlier this month. It would create enterprise zones to stimulate new business and economic growth in depressed inner cities. The concept is based on the premise that there is currently an inadequate number of jobs in America's inner cities for young, unskilled workers because the country has regulated, zoned and taxed smaller businesses almost out of existence.

Historically, smaller businesses create most of the jobs in the inner city, especially for unskilled persons. Capital for starting small businesses is traditionally obtained from savings and loans from friends, rather than through banks or the Small Business Administration. [Less than 3 percent of small companies in the United States use government aid to start their businesses.]

Representative Kemp recently explained the enterprise zone concept at AGC's convention. 'The program basically revolves around the idea of dramatically changing the rates of return in areas designated by city, State and Federal Government which have high levels of poverty, a shrinking tax base and high levels of unemployment,' he said. 'If you create an area where a businessperson could get a greater reward for starting a new business or enterprise, there would be a dramatic increase in the rate of investment and job creation in that area. There are risks involved which would be worth taking because no taxes are being paid in these areas anyway. And, you can't very well lose tax revenues when there are none coming in anyway,' he added.

In the past, when jobs were available in the inner cities, a small entrepreneur might start a firm in a rented basement and employ a few local youngsters, affording them the opportunity to step on the first rung of the employment ladder. Today, however, that same entrepeneur could certainly expect a line of Government regulators waiting for him when he opened his business—the OSHA inspector, the man from EPA and the zoning official, among others—all ready to close up his shop.

In the event they didn't succeed, the tax collector surely might. Thus the businessman would be forced to leave, resulting in a weakening of the bond that holds a poor neighborhood together.

Things would be a little different under Kemp's enterprise zones. In various areas of depressed neighborhoods, there would be drastic cuts in taxes on business income and capital gains. Incentives would also be offered to local and state government, to streamline regulations, and the federal government could develop alternative regulations as long as they did not contradict any legislative mandates. Kemp feels a climate for innovation and enterprise would be created in these zones where redtape and taxes are minimal. The results would be genuine jobs, neighborhood businesses, a sense of opportunity, and a mix of the residential and business sectors.

The entire concept of enterprise zones originated in Britain through an unusual alliance of the left and right. Peter Hall, former chairman of the socialist Fabian Society, wrote a pamphlet that inspired Sir Geoffrey Howe, the conservative Chancellor of the Exchequer, to urge that it be tried. In April 1980, despite strong opposition from the Labor Party, the conservative government provided about $70 million for six enterprise districts in England, Scotland, Wales and Northern Ireland. Firms locating in these areas pay no local taxes, receive immediate and full tax write-offs for capital investment, and avoid the paperwork usually required for government training grants.

The passage of the enterprise zone bill into law would create a possible market for municipal-utilities contractors because anytime there is physical development or building activity in a city, there is a need for bringing the infrastructure up to par to accommodate the population growth. Specific jobs might involve repaving streets and sidewalks, installing new sewers, storm drains, natural gas pipelines, water systems and other utilities. By requiring local governments to make a commitment to the proposed zone, the Kemp-Garcia bill increases the likelihood that new infrasture development will take place in these areas.

It is evident that the enterprise zone concept offers real hope to inner cities. It would not require tax money—just the opposite—it would take people off welfare rolls and turn them into taxpayers. Suspending taxes on empty buildings or unemployed workers involves no loss to a city. Even the tax loss on occupied housing and commercial buildings would soon be recovered by increased revenue as new jobs were created and economic growth stimulated. And in many ways, the most important element of all would be the psychological benefit. Enterprise zones would break the spiral of defeatism in inner cities—the feeling that the road ahead consists only of handouts and subsidies. Instead, they offer a future with jobs that provide new skills and opportunities.

In 1970, in the South Bronx section of New York City, 66 percent of the inhabitants were black or Hispanic and 40 percent were below 18. One third of the population is now dependent on welfare, and although the South Bronx has lost 20 percent of its residents, it has lost fewer than 3 percent of its welfare cases. The effect of this on the city's overall tax base is, obviously, devastating.

Representative Kemp's bill would convert the South Bronxes of the United States into enterprise zones and make them attractive to small entrepreneurs—men and women with marketable skills and optimistic ideas but little capital to implement them. They are usually willing to devote long hours in poor working conditions to build up their businesses. And, in addition, the entrepreneurs would utilize the labor of family or neighbors to establish and conduct the enterprise. Studies have shown that such entrepreneurs generally have very little knowledge of business skills when they begin. However, the entire process of establishing a business serves as an apprenticeship and as the business grows, it draws in more and more local help. These employees may commence with low-paid, unskilled work, but they can acquire skills and responsibilities as the company develops.

'So why haven't small businesses moved into the South Bronx or other blighted areas across the country?' opponents of the bill ask. The reasons for this are excessive regulations, inflation, taxes and government paperwork. The enterprise zone concept would eliminate many of these inhibitions.

Opponents also claim that cutting taxes would decrease revenue and force more service reductions. "But what taxes are collected on empty commercial buildings or abandoned blocks of apartments?" supporters ask. Stimulating new activity would probably mean an increase in current revenue and certainly in future city income, they argue.

If the concept is implemented in certain areas of the United States there would be little chance that already established businesses would relocate to the enterprise zone because special concessions would be abandoned after the business reached a certain level of turnover and profitability. Most of the business attracted by the legislation would be new, predict supporters of the idea.

Representative Kemp calls the concept a bold departure from the traditional and unsuccessful solutions normally offered to inner city problems. Unlike most of these, it would not be the beginning of yet another ever expanding flow of federal dollars. Instead it would allow the innovative genius of the small entrepreneur to be turned to the issue, resulting in private money being risked and productive jobs being created.

Many cities are already moving rapidly on the enterprise zone concept. One community in Washington, D.C. is currently examining the idea closely, but the city's administration is "dragging its feet," according to supporters of the program. Spokesmen for the Reagan administration have made it clear that the enterprise zone concept will be pushed hard—Probably as a pilot project in several cities. Obviously those cities with plans in hand will have an advantage over others. It might be impossible to implement the entire enterprise zone plan in the United States, where congressional action is hard to stimulate and local ordinances sometimes are equally tough to change. Nonetheless, the idea of private enterprise succeeding where the bureaucracy has failed is a bold, optimistic plan that's worth a chance.

CAPITAL FORMATION AND RETENTION

Options:	Chamber Position:
Replace the present corporate income tax schedule with a more graduated rate scale for the first $1 million of income.	The Chamber recommends a 15 percent rate up to $50,000 of income, a middle step at 22 percent up to $200,000 of income and a 43 percent rate above $200,000.
Adopt a simplified depreciation system to replace the present complex Asset Depreciation Range (ADR) regulations.	Chamber supports.
Permit capital expenditures to be expensed immediately rather than depreciated or amortized over a term of years.	Needs further examination.
Provide an effective jobs tax credit for small businesses.	Chamber has supported both general and targeted credits on a pilot basis; and believes jobs tax credit programs and similar programs which stimulate employment in the private sector should eventually replace existing federal programs of direct public employment.
Increase to $500,000 the allowable earnings accumulation before the imposition of an accumulated earnings tax.	Chamber supports.
Permit deferral of taxes for roll-overs of investments affecting small businesses.	Chamber supports.
Revise Subchapter S to: expand the number of shareholders permitted; to eliminate restrictions on those persons who can be shareholders; and to allow the allocation of specific items of income, expense credit, etc. to shareholders in a manner similar to partnerships.	Chamber would probably support.
Further reduce the capital gains rate.	Chamber supports.
Provide tax credits for direct investment in small businesses.	No position. This type of proposal needs careful study because of the technical problems likely to arise in determining the overall tax liability of the corporation or individual.

FEDERAL PROCUREMENT

Options:	Chamber Position:
Office of Management and Budget (OMB) should insert into the "requirements" process a small business "input" by (1) requiring the agencies to have a small business representative present when requirements are being formulated and further require his acquiescence in any decision reached during that process; and (2) requiring the approval of the Small/Disadvantaged Business Director (at headquarters or local level) under the aforementioned circumstances.	No position but appears to be excessively cumbersome.
OMB should ensure that the Small Business Administration (SBA) has adequate funding and personnel to effectively implement its responsibilities under Public Law 95-507.	Chamber supports this concept, but does not accept conclusions of discussion (in option paper) that agency needs "many times" its present staffing level.
Establish a permanent and full time Task Force in OMB to develop research and legislative proposals for two tier procurement regulations for small business, reduced paperwork and administrative burdens, etc.	Chamber supports.
SBA should incorporate procedures into the PASS system to insure its effectiveness.	Chamber supports. SBA management is responsible under current legislation.
Develop companion system to PASS which would maintain current Data Base of all planned and current procurement actions.	Chamber supports.
Large "research" and "development" programs should be divided, where feasible, into smaller parts to permit solicitation of proposals and award of contracts to small technology based firms in lieu of making a limited number of awards with consolidated requirements that only large firms can perform.	Chamber supports, with the additional criteria that the division into smaller parts be cost effective, a commercial source does exist, and national security and military preparedness are not jeopardized.
An effective Federal "set-aside" program for small business should be established for research and development contract awards.	Under study.
Require by legislation that each Federal Department and agency award a specified percentage of the agency's R&D budget to small business.	Under study.
Intensive efforts should be made by Federal agencies to reduce (or compensate for) impediments experienced by small technology based firms.	The Chamber supports continuous monitoring of the effects of regulatory policies on small business as to eliminate provisions which discriminate unfairly against small business.
The agencies, including the Small Business Administration, should use more technically trained personnel to serve as advocates for and advisors to small technology based firms.	The intent of this option is not clear.
OMB should require Federal procuring agencies to promote subcontracting to small firms through provisions in contract solicitations, source selection criteria, and negotiations for R&D work.	Needs further study and the effectiveness of Public Law 95-507 needs to be examined.

The Office of Federal Procurement Policy (OFPP) should be directed to develop (or have developed) methods to collect data on the small business share of R&D.	All reasonable and feasible data are desirable so long as the collection meets criteria for avoiding burdensome paperwork; SBA Office of Advocacy may be considered as a cooperator or alternate source of data.
Public Law 95-507 (or the implementing regulations) should require that the prime contractor set forth a narrative description of its manufacturing processes it will employ. The description should identify on an assembly, nonassembly and component basis the items it will subcontract to small/disadvantaged businesses.	Chamber opposes because of forced disclosure of proprietary information vital to the company's future competitiveness.
Establish at the level of the field or regional activity chief an Office of Small and Disadvantaged Business Utilization (SADBU).	Chamber opposes. This proposal appears to lack justification for the additional staff and budget required.
The agencies must be advised as to the requirements of Section 221(k)(6).	Chamber opposes. Each agency is already responsibile for complying with the law.
Consideration should be given to vesting in the Office of Federal Contract Compliance Programs (OFCCP), in the Department of Labor, authority to enforce and evaluate compliance, by contractors with the terms of Public Law 95-507.	Need further justification.
Develop and use an effective "breakout" program so that the large requirements are broken-down into smaller, constituent parts.	Contract requirements should be continuously monitored and, where appropriate, revised to remove all unnecessary limitations that impede the use of smaller contractors.
Reimburse small companies for their expenses in prosecuting successful claims against the Government.	Under study.
The Small Business Administration (SBA) should not interpret "economic disadvantage" in arbitrary terms.	The intent or possible effect is not clear, but the SBA should use unambiguous and uniform criteria to determine eligibility.
SBA should recognize the need to increase the flow of contracts from all procuring agencies of the Federal Government.	Chamber supports maximum reliance on the private sector for goods and resources.
SBA should foster the utilization of legitimate joint ventures between minority and majority-owned firms to increase new areas of contract opportunities.	Fully support concept, recognizing difficulties as reflected in past experience.
SBA should require "graduation" of 8(a) companies, if its size exceed the small business criteria for three consecutive years, or if the company has been in the program for 10 years.	Would support graduation concept but question whether this long a term is necessary.
SBA should allow 8(a) companies, who have been successful, to stay in the program if a percentage (20 percent) of their resource is used to assist other 8(a) firms, instead of graduating such firms.	Chamber opposes. The greatest service to strengthening minority firms is rendered by making successful companies self-reliant and allowing programs to assist other, smaller firms.
Develop and enforce the OMB's A-76 ("contracting-out") program to assist small and minority business.	Chamber supports.

Mr. **Mitchell.** I think it might be fruitful if we would take testimony from all in the panel before we ask the questions.

Mr. Tang, please proceed.

TESTIMONY OF EDMUND TANG, MAYOR OF PEORIA, ARIZ., MEMBER OF THE CHINESE CHAMBER OF COMMERCE

Mr. TANG. Thank you, honorable chairman.

My name is Edmund Tang. I am the mayor of Peoria, Ariz. I am a member of the Chinese Chamber of Commerce and have served as president of the Peoria Chamber of Commerce. I am on the board of directors of the Associate Grocers, Arizona only, and Retail Grocers Cooperative Wholesalers, and have recently been elected to the State board of the Arizona Retail Grocers Association. I am a small retail grocer.

At this time, I will make my presentation on behalf of the Asian coalition.

The Small Business Administration was created to serve a social and economic purpose: That the health and vitality of this Nation could be served best by encouraging the growth and development of small business. The encouragement of minority-owned small business reflects an extension of that policy. This committee is here today to hear testimony relating to the problems of small business and to seek solutions.

We, as representatives of various Asian groups, are here today as members of the Asian coalition. We present to this committee this paper describing what we feel are the problems and possible solutions. It is our contention that small business faces three major problems which are within the jurisdiction of this committee. The three problem areas are: One, funding, direct and guaranteed; two, procurement contracts; and three, management development.

The first problem area, funding, presents the single greatest challenge to small business. Small business cannot begin or survive without adequate sources of capital. The large failure rate of small business results most often from thin to wholly inadequate finances. A major function of the SBA has been to provide small business with capital. In this area, however, the long timelag between loan application and loan approval to the final receipt of funds has made the SBA loan procedure unreliable in the business world. Business opportunities require certainty on both sides. There can be no effective transfer from seller to buyer unless both parties can speak with a definitive voice. Presently, the buyer who depends on SBA money to provide the seed capital is at a competitive disadvantage with other buyers of the same business.

We feel that this problem may be addressed in several ways. First, instead of the present requirement of two bank denials, the SBA should encourage and help the local banks form a joint bank committee solely for the purpose of reviewing SBA loan applications. The banks could underwrite small business loans on some type of pro rata basis. The SBA would then guarantee, if approved, loans that were rejected by the banking pool.

The present committee approval method should be changed somewhat. Instead of the present document preparation which involves detailed and cumbersome paperwork, there should be some type of preliminary application. This application would be short and would highlight the essentials of the business opportunity to be sought. Here, the SBA could set up certain guidelines which would determine feasibility based on an initial set of criteria. This would have the effect of weeding out certain loans which would be automatically suspect because of high allocations for intangibles, such as good will, which would not necessarily be as valuable as transferred.

In addition, the present administration has committed itself to the formation of free enterprise zones. We feel that the SBA could be very instrumental in the development of these zones. A municipality could designate an area for revitalization and growth and then request that the SBA aid in business development. In such an area, the SBA could designate certain fast track loans. These loans would have fewer constraints and greater approval chances.

With respect to this issue of funding, a particular concern of Asians is the language barrier to loans for immigrants. The SBA could aid in this area by having an Asian liaison whose primary function would be one of assistance in handling the communication gap.

A second area of Asian concern with the SBA involves the present procurement system of Government goods and services as well as Government funded projects. Asians in the past have been unaware of their opportunity to bid on these various projects.

Furthermore, there does not exist at this time any review within the SBA of these Federal contracts. We feel that there are contractors who hold Federal contracts and who do such a large volume of business that they cannot be fairly considered a small business.

We suggest that the SBA set up a review committee. It would review Federal contractors on two criteria: duration of the contract and the percentage of the contractor's gross receipts attributable to Federal contracts. A time limitation would insure that no one contractor held a monopoly on a certain Government contract and would permit others to enter into the bidding.

A gross receipts limitation would insure that no one contractor derived so much of his business solely from Government business. Again, this would encourage every grantee of a Government contract to pursue other business and not stagnate.

The third area of concern involves management development. To those who would start a small business, Government regulations are often a very significant barrier to operation. In addition, there are always ongoing regulations which the operator may not be aware of. While the SBA has a group—SCORE—which serves many useful functions, that group does not necessarily have all of the basic working technical knowledge involving each and every governmental regulation which affects the startup of a small business, as well as the regulations which affect the continued operation. The SBA could perform a very useful service simply by compiling lists, by business type of those Federal, State, and municipal regulations.

Along the same line, there are various technical and skilled labor pools which exist to provide the necessary labor force for certain businesses. Often, the operator does not even know that these pools of skilled labor exist. The SBA could go into the community and develop various lists and contacts for the operator to seek for assistance.

Finally, again a particular concern of the Asian community is this problem area deals with the language barrier. The SBA could lend assistance by aiding in various language programs and expanding the present English as a second language program.

In summary, the Asian community feels that the SBA performs a very useful function and that its aid more often helps a small business person to stay in business and avoid failure. The problems we have outlined are within the realm of the SBA purview and can be solved by the SBA.

On behalf of the Asian coalition, I wish to thank this committee for this opportunity to appear before you today. I wish also to commend you for holding a field hearing, which type of hearing is a unique opportunity for government to talk to the citizenry at the most local level and the citizenry to see government at work at the local level.

Thank you very much, Mr. Chairman.

Mr. MITCHELL. Thank you, Mr. Mayor.

I do have some questions for you. I will just hold them until we hear from our final witness in this panel. That is Mr. Carl Hamilton, the president of the Arizona Black Chamber of Commerce.

TESTIMONY OF CARL HAMILTON, PRESIDENT, ARIZONA BLACK CHAMBER OF COMMERCE

Mr. HAMILTON. Thank you.

To the Honorable Parren J. Mitchell, chairman and the honorable members of the Committee on Small Business, thank you for this opportunity to speak before you.

As president of the Arizona Black Chamber of Commerce, I represent a percentage of 231,000 businesses which the Small Business Administration has pointed out as owned by black Americans. The Arizona Black Chamber of Commerce is concerned with the unique problems of black small business persons locally and nationally as they have made and are making their impact upon the individual black and minority businesses here.

Does the free enterprise system work for the black business community in America? Problem areas that face the black business community fall into the following categories: (a) New business startup; (b) survival; and (c) growth and development.

I will address each of the above problem categories and some of their ramifications and make recommendations for solving some of the problems involved. The comments will be mine as we go along.

Before going any further, I would like to redefine the term "minority" as it is used in business and Government specifications. There should be a standard, uniform definition of the minority. A minority should be defined as one who is easily recognized as such visually and is accepted by the members of this ethnic group in the community.

A person who can pass as a member of the majority ethnic group and who must produce documentary proof that he belongs to a minority ethnic group should be excluded from classification of minority. It is frustrating to be blown out of competition for a job or contract by a passer who only uses the designation of minority when it is expedient.

Also, I recommend dropping the term "disadvantaged," as it tends to shut out minority businesses. Congress should make these changes in definitions in order to clarify intent, meaning, and terms, and thereby bringing about the desired results. It is high time that some of the specific committees, councils, that are made up of so-called ethnic members of the community that do not represent the interests of small business, of black business, should be removed from the particular councils and boards which they serve.

Mr. MITCHELL. That is at all levels?

Mr. HAMILTON. At all levels.

Mr. MITCHELL. Local, State, Federal?

Mr. HAMILTON. Yes, sir. If they are not responsive to the need, they should not be on the board, or council, or whatever it may be.

The high rates of unemployment and underemployment among blacks, coupled with the advertisements and publications that major Government prime contractors use, supposedly in a sincere effort to identify and utilize minority venders attract and encourage large numbers of first generation black business into existence. Without that, a large number of us would not have quit our very secure, low-level jobs and joined the free enterprise system.

These new black businesses use every means available to them, including borrowing from family and friends to enter into business. They start up with high hopes, but lack of utilization or underutilization dims any such hopes and their businesses soon fold. No matter what your product or service is, if it is not utilized, you will not be here.

Black businesspersons are a vital economic resource to be discovered, developed, and utilized here in Arizona as well as nationally. If this portion of our human and economic resources would be utilized to its full potential, it would create new jobs for the residents of our cities, create new revenues, and generally decrease the incidence of unemployment and underemployment that have contributed to the perpetuation of the continuing cycle of poverty among blacks and minority peoples.

Black business people hailed the passage of Public Law 95-507, the law designed to assist the survival and development of socially and economically disadvantaged businesses, with joy. But then they could see the sophistication taking place in industry that resulted in the hindering of blacks and other minorities from receiving the benefits this law was designed to bring about.

We are very much concerned about major companies in the valley, and also in the State of Arizona, that merely put officials, not necessarily even officials, but members of their company on boards and commissions in the State of Arizona, again in an attempt to be visible in the overall community, but have no authority or no full commitment to the advancement of black business issues. There is no sensitivity and no awareness. It is merely an effort to be visible.

The economic survival, growth, and development of black businesses can only be achieved and further developed by the incorporation of black businesses into the mainstream of our State and national economy.

The joint venturing dialog between black business and Congress that would result in the formation and implementation of a Federal mandate against Government prime contractors who have subcontracted with minority firms only to comply with the law but apply such restrictions and hindrances as to cause the black contractor to fail in fulfilling such contracts. Again, you may land the contract, but harassment on the job in fulfilling that contract generally drives the black business away from the contract.

Mr. MITCHELL. May I interrupt at that point. I will try not to do this again. Would you give me a specific illustration of the kind of harassment that you have looked to?

Mr. HAMILTON. Upon winning a contract with a major firm, the supervisory staff that you interface with, your company interfaces with, creates pettiness with your staff that is working on that particular site.

Mr. MITCHELL. OK. Could you dig a little deeper than that? Pettiness—some specific things?

Mr. HAMILTON. We have one illustration that was brought to my attention recently of a janitorial firm that had cleaned up the building properly, and it was turned in and reported as having not done the job properly. Upon going over to the job site to review what happened, they noticed all the furniture had been moved. Where the furniture had been sitting, there was some debris. These are the types of harassment, that we would call harassment. The contract called for cleanup in the open areas, but the furniture had in fact been moved, and it was identified as a poor job.

Mr. MITCHELL. Why don't you go ahead with your testimony. But I do want to pursue this a little bit later on.

Mr. HAMILTON. Yes. I have some very interesting personal experiences over the last 8½ to 9 years, working with major prime contractors in the State of Arizona that I feel are atrocious and an affront to the total Public Law 95-507, in which—further in my testimony—I feel there should be indictments.

It is important that proper monitoring and enforcement procedures be put in place to prevent improper tactics and that the monitoring and enforcement personnel have the authority to impose punitive sanctions so as to achieve the results desired by the letter and the intent of the law. Big banks in our State choose to be part of the problem as opposed to working toward a solution. They are profitmaking organizations. Their profits are guaranteed through SBA's effort. Still, they find it incumbent upon themselves to not provide equal access for the black business people to capital. I underline here the big banks.

The limited success of the set-aside program through the SBA 8(a) program suggests that there is a much larger problem hidden beneath the tip of the iceberg. There are less than 25 8(a) participants in all of Arizona. Our concern here, the program that is really intended to help small businesses to grow and survive in a State with as large a number of businesses as Arizona has, finds only—in the 8(a) program finds actually 24 8(a) set-asides. This really brings concerns to us that this program has not expanded and has not developed further to make it a meaningful program. Time and effort has to be expended in this particular program and it only impacts on a small percentage of the total State population.

The requirements of DOD and other governmental agencies using 8(a) companies suggest the presence of traditional racism when investigating the business categories in which these certified participants are engaged. Generally janitorial firms in Arizona, a few contractors, and I think two consulting firms. The nontraditional black business types or categories, if you will, are not certified in any numbers in this portfolio of 24, 25 certified firms.

Thus, hundreds of thousands of dollars in Federal defense and other governmental agency contracts are lost by certifiable, nonstereotyped blacks in the State of Arizona. That concerns me very much.

Capitalism has thrived as a system because profit is the means by which the rewards of effort can be measured. But in the contract system, as it is being used on black non-8(a) firms, it is impossible to make a profit with contracts that are awarded by competitive bid. Contracts are awarded to companies, it appears to me by my calculations, that the contract price is below the cost of my labor. There is something wrong.

Arizona to date has less then five minority printers within the State. Of this number, two are black. Problems in this industry range from lack of financing for badly needed equipment—expensive and ever-changing equipment—and limitations on marketing capabilities—namely, the ability to publish various mass audience-appealing periodicals that would allow for the necessary funds to run the main printing operation. We are told that the SBA does not guarantee direct or indirect loans to this particular industry.

Black printers should be given similar privileges as persons seeking radio and television station financing, and consideration should be given to black printing operations under the 8(a) program. Since military publications are printed in this area, it would be conducive to have black printers accomplish these tasks.

Specific suggestions are as follows:

One, that persons who invest in minority-owned businesses be given a tax credit equal to the amount of their investment.

Two, that minority-owned businesses should be given additional tax credits for the purchase of equipment for the employment of minority individuals.

Three, that profits generated by a minority-owned business should not be taxed if such profits are reinvested in the business.

Four, that the State should establish a revolving fund financed by at least 50 percent of all sales taxes collected from minority businesses. Provision thereafter should be made to allow any minority business within the State to borrow from that fund at reasonable interest rates. Administration of the fund should be accomplished by a commission specifically established for that purpose, which includes adequate representation from the minority business community.

Solutions and recommendations:

One, the public laws, rules, and regulations have not been complied in accordance with their intents and purposes. To encourage a flow of capital to minority and black firms, we recommend that Congress offer tax incentives for businesses who do a reasonable percentage of their business with minority or black firms.

Two, Congress could encourage new black and minority businesses by offering them a moratorium on Federal taxes for 10 years if it would be reinvested in their business.

Three, sanctions should be enforced at the monitoring level up to the chief executive to insure complete compliance of the rules and regulations governing equal opportunity for minority businesses.

Four, the chief operating officer or the Government contractor that violates or circumvents Government and/or MBE procurement requirement should be levied fines and prison sentences as deterrents of circumvention or breach of those procurement laws and regulations.

Five, Congress should encourage banks and life insurance companies to develop creative minority business development loans by tax rebates, discounts, et cetera.

Six, sources of short-term loans—90 day maximum should be available. We are consistently hearing of long-term loans. A lot of the businesses that are fast tracking do not need a long-term loan—5, 6, 7 years—but 90 days or less. In fact, now there isn't any particular area in which this can be addressed. It is a problem in our particular industries in which we serve. Short-term money is very, very critical.

Seven, that State and federally chartered financial institutions be required, as a condition of receiving or maintaining their charter, to engage in affirmative lending practices to minority-owned businesses and that records be maintained on this effort and are published at least annually.

Eight, that any financial institution which competes for the deposit of Federal funds be required to develop an affirmative action lending program and that such programs be evaluated as a substantive element of the Federal selection of any financial institution to act as a depository for its funds.

In conclusion, the problems that black persons face in the startup, survival, and growth and development of their businesses are not insurmountable if all concerned could understand these problems and work toward their solution. The monitoring of the program to help black businesses can be effective only when the results can be measured in economic and quantifiable terms.

Economic parity for the minority and black business community is the purpose and objective of my testimony. Therefore, in conclusion, be it resolved:

One, that the Congress redefine the term "minority" so as to include only those who can visually be seen as belonging to a particularly ethnic group and are accepted as such by other members of the particular group, excluding those who visually seem to belong to the majority ethnic group and need documentary proof of membership in such a minority group.

Two, that the Congress drop the term "disadvantaged" as it tends to shut out minority and black businesses.

Three, that the Government shall continue to practice the principles of utilizing small and minority-owned businesses to the greatest extent with economic parity as its objective. The proportion of Government dollars spent for products or services should reflect the composition of the population it represents.

Four, that the Congress shall enact such economic incentives as tax credits for those majority businesses utilizing black and minority businesses and shall impose fines and jail sentences upon the executive officer or officers of Government prime contractors who do not so utilize black and minority services and products in parity with the composition of the minority population in the country.

Five, without these incentives, sanctions, and deterrents, all attempts for economic parity by black and minority businesses are merely dreams that they cannot see realized.

Six, the Arizona Black Chamber of Commerce is committed through the Governor's Office on Small Business to work with the Governor and the State legislature to encourage and promote purchasing procedures, policies, regulations, and laws favorable to the development of black and minority businesses throughout the State.

The State of Arizona does not have a procurement plan that is again sensitive to the needs of minority businesses. As far as I am personally concerned, if legislative mandate fails to achieve a positive and immediate means of minority companies survival, growth, and development, we will be forced to revert to animal behavior just to survive.

We will survive. We will grow. We will develop. That is the pursuit of my happiness.

Thank you.

[Mr. Hamilton's submitted exhibits marked A, B, and C follow:]

EXHIBIT A

To establish G. Buse & Associates as an Electronic Data Processing (E.D.P.) Consulting Association, I have attempted to secure the necessary capital through the S.B.A. under the E.O.L. Program.

I approached the S.B.A. in early 1980 with my business plans and I was sent to the Phoenix Small Business Development Center (P.S.B.D.C.) to have my business plans put into "formal loan proposal package form". Upon arrival at the P.S.B.D.C., I was informed that I would have to transfer all information, that I had compiled, onto Official Forms. This to be done by myself or I could wait several weeks until someone was available to assist me. I was given several forms to complete and return. When I returned the completed forms I was informed that there were other forms also that must be filled out and returned. Once again, I completed the forms and returned them and once again I was given forms to complete and return. This sequence continued until I was informed by letter that the P.S.B.D.C. could not prepare a loan package unless it met certain guidelines as required by Contract with M.B.D.A. and U.S. Department of Commerce.

Once again the rules had been changed and I could not qualify under these New regulations.

I voiced my displeasure with the way I had been treated/handled by the P.S.B.D.C. at a Small Businessman Conference sponsored by the Black Chamber of Commerce and my complaints were heard by Mario Correll. I was then informed that the situation would be investigated. Shortly there after, I was introduced to Mr. Joe Galvez, who was to assist me in preparing the Formal Business Loan Proposal which included a profit & loss projection, market survey analysis (conducted by myself), forcast rationale, and other information requested from previous meetings with P.S.B.D.C. and once again I was informed

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that other information would be necessary if the loan proposal was to be submitted to the S.B.A. for review. I was also informed that the profit & loss projection and cash flow schedules would have to be changed because the S.B.A. would turn down the Loan Proposal because the Profit & Loss projection indicated that the business showed no profit after the first year. I argued the point that the projection reflects real profit & loss as I saw in terms of sales and service from a realistic (accountant's) projection.

All information requested was promptly submitted and on March 24, 1981 the Formal Loan Package was submitted to the S.B.A. with all requested documentation. Several weeks later, I received a letter of declination.

I promptly notified P.S.B.D.C. that the proposal had been rejected and that I was confused as to the reasons of its rejection.

I am concerned as to the purpose of the S.B.A. and those other organizations set up to assist the individuals that have a desire to own and operate his/her own business. There seems to be a definite communication gap between the Federal Government (S.B.A) and those private organizations funded to assist the S.B.A. in preparing those documents necessary for consideration of a loan proposal.

I personally feel that if P.S.B.D.C. is to assist the S.B.A. there must be a better exchange of information as to what information is necessary.

My questions are therefore: What exactly are the guidelines? How many changes in those guidelines is a person to expect? How is one expected to readily prepare for them when one isn't apprised of them?

Proposed Solution: The most immediate problem being communications between the S.B.A. and P.S.B.D.C.

If P.S.B.D.C. is contracted to prepare the Loan Proposals they should be constantly up-dated as to the guidelines according to the S.B.A. If they

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cannot prepare a package to meet S.B.A. guidelines, why waste the tax payer's money funding an organization that is misinformed, uninformed, or simply not doing its job? On the other hand if P.S.B.D.C. has been preparing loan packages according to old S.B.A. guidelines, they should be advised of the new guidelines.

There are people within the S.B.A.'s organization that could also be used to bridge the communications gap between the applicant, the S.B.A., and P.S.B.D.C. Those individuals employed by the S.B.A. to assist the Small Bus-Operator, whether its an established business, or a start-up business, could/should be delegated more authority in the decision making process and with assisting in business development. There are those within the S.B.A. who have no authority to advise, or counsel, prospective business operators.

As for the rules as specified by the S.B.A., if the applicant is aware of the guidelines he or she is less likely to fall prey to erroneous information and more likely will be within the guidelines set-up by the S.B.A. That would make it less confusing and give better chances to everyone.

Submitted by: Grady Hore

EXHIBIT B

The Arizona Center for Corporate Responsibility is a non-profit organization formed to monitor the behavior of Corporations and Banks located in Arizona in the areas of corporate responsibility, i.e. equal opportunity lending loans to South Africa and pollution.

Since early 1980, ACCR has been concentrating on getting the Arizona Bank to institute a meaningful and non-discrimination program toward black and other minority businesses. With total assets of $2.2 billion dollars and 92 branches, the Arizona Bank is the third largest state chartered bank in the Southwest.

ACCR was very disturbed to learn from the SBA and the Farmer's Home Administration that the Arizona Bank had only extended one loan to a black person for only $35,000 through SBA and none through the Farmer's Home Loan Administration from January 1, 1976, through May 31, 1980. Although we were unsuccessful in getting the bank to disclose its non Government Guarantees to blacks, we have reasons to believe the bank made few, if any, non-government guaranteed loans to blacks. This is particularly true in that the Bank continuously emphasized that it is very conservative in its lending policy. This position was again articulated by Don B. Tostenrud, Chairman of the Board in his May 1981 presentation before the New York Society of Financial Analysts.

In September 1980, a community organization, Arizona Association of Community Organizations for Reform Now (ACORN), filed a protest with FDIC in San Francisco over housing discrimination by the bank in low income and minority areas and for not having a branch in that area. After discussions with ACORN over a 3 month period, the bank agreed to put a branch in South Phoenix and provide counseling to the residents in that area in exchange ACORN agreed to drop its complaint. ACCR's analysis of the bank's proposal for a branch in South Phoenix raises serious questions.

Because of the hostile feelings toward ACCR, the bank refused to address the minority lending aspects of our complaint. ACCR encountered equally hostile treatment by Mr. Charles E. Doster, Regional Director of FDIC, and Mr. Ford R. Paulsen, Regional Counsel. We expressed our concern to Mr. Roger Hood, Assistant General Counsel, FDIC, who responded conscientiously to our concerns. ACCR thoroughly agrees with Ralph Nader's statement "No regulator has been as prone to prostrate themselves before the vested interests of the regulatees as have banking regulations".

ACCR recommended that the Federal Government enact the following laws:

1. Every financial institution be required to file a detailed financial plan for lending to minority businesses along with goals before obtaining direct or indirect federal deposits.
2. Every financial institution should be required to publish annually the number and the amount it loaned to various minority businesses.
3. The Federal Government should require that every financial institution present a detailed plan along with goals concerning the use of black and other minority contractors and sub-contractors in the construction of branches, facilities, etc. before their application is approved.
4. Before receiving approval for applications, every financial institution over 100 million in assets should state the number of minorities on its board. If there are no minorities, it should state its policy on recruiting minorities for its board.
5. Congress should frequently monitor the responsiveness of the banking regulators to the general public and monitor their fraternization with the regulatees.

Submitted by: Marvin E. Perry, President
The Arizona Center for Corporate Responsibility (ACCR)

EXHIBIT C

As tax paying citizens of these United States, I am sure that we are all interested in the U.S. Government purchasing agencies buying goods and services that are reasonable in price and as high in quality as possible. I'm sure this is true, no matter who the suppliers may be.

However, I am particularly concerned as a small minority business person about how the U.S. Government Procurement agencies work for us, in terms of Small Business set asides, the bid process, bid bond, performance bonds, length of contract, and the definition of "lowest responsive bid".

First, the small business set asides. The term Small Business is defined by the Government as a business with gross annual receipts amounting to no more than 4.5 million dollars. It is awfully difficult for a business with gross annual sales of under one (1) million or even less to compete.

Second, The bid process. It has always puzzled me as to why the Government procurement agencies allow contractors to submit bids that are far too low to accomplish the required work. Why doesn't the procurement agency, since they are aware of what is required, what the contractors' cost are, the man hours required, and the quality of service required, have minimum quotes that are acceptable? In other words, why allow contractors to go in and fail? This is particularly true with small inexperienced contractors, who make up the bulk of the bidders on these contracts. It appears to me that the elimination of very low bidders or bidders who will probably not be able to supply the goods or services, should be the first order of business for the procureror. It stands to reason that a supplier who can't show a profit because of an extremely low bid, cannot or will not do the job. What does it cost the government to bid out the same goods and services every year? If in fact the federal government wants to assist the small minority business it would certainly appear to

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me that it would take longer than a year to accomplish that. Or if true assistance is the intent, it would also appear that the procurement agency would allow the contractor to make a decent profit and not have to compete with much larger companies. In short, the present system seems to place the federal government in an "adversary" role rather than in the role of assisting small or minority businesses. I'm sure that any contractor who does business with private industry or the federal government realizes that he must perform or not do business. The federal government appears to be in a great position to take advantage of these small business persons by having stringent rules and regulations and even threatening to levy heavy cost on these contractors when they fail. It is my opinion that this attitude should be changed to one that is more supportive of small and minority businesses.

Additionally, the bid and performance bonds required on some of the larger contracts prohibit many small capable contractors from participating in the bid process. Adequate references, credit reports and a small Bid Bond or performance Bond would encourage more participation. As to the length of the contracts being awarded - one year in most cases, without any options. It would certainly seem that on contracts requiring large payrolls and benefits and particularly where the bidder is successful in obtaining a contract where he/she inherits the former contractors personnel, sick leave and vacation are also inherited, thus adding more up front costs. By awarding contracts for a one year period with an option that may be exercised by negotiation or a two year contract with no option, the contractor at least has the opportunity to recap his investment under this kind of system. Of course this would only work if the contractor provides adequate service.

Respectfully submitted by: James A. Johnson
White Glove Services, Inc.

Mr. MITCHELL. Thank you very much for your testimony and the testimony of all the members of the panel.

Before asking some questions, we have got some housekeeping problems that we have to clean up. Almost inevitably, it has been my experience when we go around the country we get off schedule. Witnesses take a little longer; we raise too many questions.

We are required or forced to break at 11:30 and resume at 1:30. What I would like to do—let me get a lead from the panel of the 8(a) firms—Mr. Day, Mr. Ruiz, Mr. Gray, and Mr. Alvarez. Can you make it back at 1:30?

Fine. I wanted to resolve that problem. I assure you that every person who is slated to testify today, we will hear, even if we have to extend the afternoon time from 4:30 to a bit later. There is quite a bit of testimony.

I must say, Mr. Hamilton—you are kind of a tiger, aren't you?

Mr. HAMILTON. We must survive. We will survive.

Mr. MITCHELL. All right; let me get to some questions here.

Mr. Parra, in the testimony, when Government agencies do not enforce the subcontracting plan portion of the law—that is, the Department of Transportation—can you give us an illustration—this is on page 4 of your testimony—"it is a wonder the prime contractors don't, either." What do you mean by this? What has the Department of Transportation done or failed to do?

Mr. CASTILLO. Well, Mr. Chairman, the Department of Transportation held a meeting here the first part of this year. They have come out with a handbook. They have gone out to many minority firms and asked them to substantiate the fact that they are minority firms. My firm has gone through that. We are doing business with ADOT.

At the present time, however, there is nothing taking place. They have hired an affirmative action officer. About 6 months down the road, all we are hearing is lipservice—contracts or requests for bidding out. As far as I can tell, not all these minority contractors get the opportunity to bid on them. When they do, they are excluded by the very definition of the bid, by the very description of the bid.

I am in the drafting reproduction business. We sell engineering supplies and so forth. Half of the bids that come through, even though they are using some Federal funds for the design and so forth in a document, we are completely left out in the competitive bid.

Mr. MITCHELL. All right. I must say that I am in firm disagreement with your recommendation that the Small Business Administration be given the power to enforce the sanctions under Public Law 95-507. In 10 years, I have seen good administrators and bad administrators of the Small Business Administration. I have seen it as a political instrument, and I have seen some people who are very, very dedicated.

I would be very wary of the central SBA serving as the enforcement mechanism primarily because I have had enough testimony in Congress, in Washington, and out in the field, to indicate that SBA really isn't doing its full job in Washington in terms of getting the procurement contracts from the other agencies. So if it is not doing its own part, I would be very wary of allowing it to become the enforcer for the implementation of Public Law 95-507. Maybe some field offices or regional offices might be good, but in Washington, I don't think that is a very good recommendation.

Mr. Tang——

Mr. **Castillo**. Mr. Chairman, I have been a city councilman, State senator, for 6 years, member of the board of supervisors in Pima County. I have seen good and bad politicans. That doesn't mean that the legislative process shouldn't continue. I think what we are saying is that somewhere the responsibility has to be laid and there has to be an enforcement agency that will try and do the job.

Mr. **Mitchell**. OK. We are absolutely together on that. I think there has got to be a central source of accountability, but I would not at this juncture see SBA as that central source. You are dead right, there is too much of the concept of basketball in sport from one person to another, and this is the kind of thing we have discussed earlier with Mr. Trimboli's testimony, and I think Mr. Hatcher had some discussion with him on that. But certainly there has to be one central source. I just don't feel it is the SBA right now.

Mr. **Castillo**. The thing is, we sit here, small business people—I had occasion just last week, I called the Department of Defense down here that is supposed to help us. He didn't know anything about the helicopter facility coming out by Hughes Aircraft in the valley. I called SBA. They tried to be very helpful. They didn't have much information.

I am in touch with Washington through Senator DeConcini's office. I am finally starting to get some information, but there is very little coordination between what is happening here at the local level and back in Washington.

Mr. **Mitchell**. That, I have heard, is a complaint in other portions of the country. And I think that complaint, that problem, is attributable to only one source, that is, the central source. If the captains in the Army or the commander don't know that a significant change has taken place in Army regulations, the ultimate responsibility goes all the way back to the Secretary of the Army. It is his job to get that out there.

I just feel that this is something that Congress must do. That is one of the reasons we have oversight hearings of the agencies in Washington, to try to force these agencies to do that which is right.

Mr. Tang, I am just a little bit curious about the Asian coalition. Who are its members?

Mr. **Tang**. It has been recently formed. Filippino, Korean, Japanese, Chinese. That is all at this time.

Mr. **Mitchell**. How long has this coalition been in existence?

Mr. **Tang**. Recently. We have talked about the fact that we need to combine our efforts. We all have the same problems, but no true spokesmen.

Mr. **Mitchell**. OK.

I have some questions for you, Mr. Hamilton. I don't know whether I am exceeding my jurisdiction as chairman of this committee in a field hearing when I would make a recommendation. I don't know, but I will make it anyway.

You have an Asian coalition. That has come into being primarily because you felt that the Asians have not gotten even their fair share of the economic development. There is a black chamber of commerce. There is a Mexican American group. I am wondering—let me play it safe—I am wondering if you would consider, and other groups consider, what the potential impact of the unification of all of these minority groups, a coalition of all of these minority groups, I am skating on thin ice, I think. I am just wondering whether you would consider the potential impact of all of these groups coming together in a coalition, to press as a common front for greater participation in the economic development process? Don't answer, please. Just consider it.

Mr. HAMILTON. It is in place.

Mr. MITCHELL. OK, then. I think it is something you should really consider. Most times we operate under the theory there is strength in numbers.

Mr. Hatcher, do you have some questions?

Mr. HATCHER. Yes, sir.

Mr. Hamilton, the question of members of a minority group who have to prove that by documentation, is that a real problem, a sizable problem in Arizona?

Mr. HAMILTON. That is the problem. That is the total problem. It would eliminate a lot of other problems, such as certification problems. The intent, as I understand it, as it impacts upon me, is when I go in the doorway of a prospective client, major Government contractor, and my black shadow casts upon the floor, I am treated immediately differently because of my appearance.

A fellow businessperson who happens to be Anglo, for example, is immediately addressed totally different, such as "good morning, sir, may I help you?" It is merely the visual cues that elicit that particular reaction, only because of our personal appearance. So the passing of unified definition of minorities, I think would really solve a lot of the other problems.

Mr. HATCHER. I was interested to see that you would recommend dropping the term "disadvantaged." How does that work in practice to the detriment of other minority businesses?

Mr. HAMILTON. As we go out on bid for procurement contracts now, everybody and their brother is now disadvantaged. Again, we only have a small portion of a pie, and they put us in a position of a bunch of us fighting over a bunch of little crumbs. We are concerned. I think if you limit to the intent, as I see it, to make viable the legitimate, real persons in need, which are small businesses, which are basically minority businesses, then removing the word disadvantaged removes all of the other individuals from competition with that special interest group.

Mr. HATCHER. Thank you.

Mr. MITCHELL. I have a question. I said that I would put my questions to you. I have almost a totally negative reaction to those two recommendations. If indeed you are accorded that kind of negative treatment when you are seen as a black person, then it seems to me that is all the more argument for clearly identifying a minority in the law so that that minority can be protected. It just seems to me by dropping the definition, you leave yourself totally vulnerable and totally open—every ethnic group represented in this panel.

By way of illustration, if you walk into any Government agency and say—and we have dropped the term minority—and you say look, I am good, I want to compete, and this guy says in his mind, look, you are a minority, I am going to listen to you but not give you anything. Unless we have some protection in the law, you are dead.

I feel the same way about dropping the term "socially disadvantaged." I see what your problem is. Your problem is the abuse which might be associated by persons distorting the term "socially disadvantaged," or distorting the term "minority." But by leaving them out, you are just a little lamb out there surrounded by a pack of wolves.

Mr. Hamilton. Correction. Not delete the word minority, delete the word "disadvantaged." But redefine the term "minority" to follow the appearances. As these people appear here, obviously they represent ethnic groups.

Mr. Mitchell. You know, in most of the legislation, when we use the term "minority" it is pretty much spelled out what constitutes a minority. For example, when we talk about minorities in various pieces of legislation, we are talking about blacks, Hispanics, Asian Americans, Aleuts, and so forth. Generally, in every piece of legislation I know of, there is a spelling out of what constitutes a minority.

Mr. Hamilton. My concern here is those that have to be certified. If one has to come in with a piece of paper certifying him as a minority, that is my basic concern.

Mr. Mitchell. I understand what you are saying. You are trying to protect against abuse. For as long as there are greedy people in the world, they are going to try to bend programs and distort meanings for their own advantage. I will simply cite when we had the 10-percent set-aside under the local public works program, we had an instance of a blond, blue-eyed, obviously Scandinavian-type coming in saying "I claim I am a minority", that he had some Indian blood or something in him—some Black blood, and he said "I am a minority." I think he was just avaricious enough to change his blood history to try to get at that money.

We have some tests to deal with that. We say where do you go to church. So you just cannot deal with the greediness of men and women to be found when there is a little to be gained.

On page 3 in your testimony, you refer to large Government prime contractors, who subcontract with minority firms only to comply with the law, but apply such restrictions and hindrances as to cause the black contractor to fail in fulfilling such contracts.

Spell out for me, if you will, restrictions and hindrances as clearly as you can, because this gets to be very difficult for the committee and for the Congress. We take your words at full face value, but then we have got to know precisely what they mean. Could you give me some specific illustrations?

Mr. Hamilton. OK. To give you one that comes to mind would be a contract with Motorola, Government Electronics Division.

Mr. Mitchell. What happened?

Mr. HAMILTON. A situation where in its annual contract, certain requirements are parceled out to different FTA awardees, if you will, of the contracts. When it comes to the black firm that is in this particular group, certain specific requirements are placed in that organization only to the minority firm.

Mr. MITCHELL. When you talk about restrictions and hindrances, are you suggesting there are some companies which, when they put out a contact, will have one set of criteria or requirements for other than minority firms, and another set for minority firms—the other set for minority firms being more stringent, more arduous?

Mr. HAMILTON. All the other what we would call specific little games that are really designed to make you ineffective, unable to perform a contract, and then consequently, you have to drop the contract.

I think of other contracts, again where the supervisory people, staff people interfacing with you, will do everything they can to make you look bad.

Mr. MITCHELL. They would verbally tell you that?

Mr. HAMILTON. Deliberately tell you that.

Mr. MITCHELL. Has that been your experience?

Mr. HAMILTON. Yes. I have had these experiences which I would be glad to document in great detail, my personal experiences, which are really atrocious.

Mr. MITCHELL. I certainly wish you would document it for this committee. To me, it is contemptible for a prime to deal with a minority and say, look, we are going to do everything we possibly can do to make you look bad or to hurt you. That is despicable.

I cannot do much about it unless you can document it. If you do document it, I guarantee you—and I think the members of the committee would work with me on this—we will do everything possible against a company that employs that kind of tactic.

Mr. CENTNER. Thank you, Mr. Chairman.

Mr. Marriott shares your concern about the enforcement of Public Law 95-507. I was thinking part of the problem is there are no property rights, so to speak, in the program. Class action suits were made possible by investing, for legal purposes, property rights to a group rather than an individual. Why not rewrite Public Law 95-507 and write in a presumptive penalty of so much per day to any agency which ignores it or violates it? In fact, if you want to dig them a little bit, instead of transferable to the Treasury's general revenues, you can make it transferable to the support of the 8(a) program and say for the purposes of the law, that the 8(a) program has been damaged?

Mr. MITCHELL. That is an intriguing idea.

One of the reasons we have these hearings is precisely for the reason—to go back and look at the legislation and see what we can or cannot do to strengthen it and make it more effective.

I want to thank all of the participants this morning. You have been really helpful. I have learned quite a bit. You generated some new ideas.

Mr. Hatcher, do you have any comment before we recess?

Mr. HATCHER. No; thank you.

Mr. MITCHELL. Then we will recess until 1:30, back in this room.

[Whereupon, at 11:30 a.m., the committee was recessed, to reconvene at 1:30 p.m., the afternoon of the same day.]

AFTERNOON SESSION

Mr. MITCHELL. The hearing is now ready to resume.

I want to thank all of you who have come back for the afternoon session. I especially want to thank all of the witnesses who have been kind enough to agree to wait through the entire session. We intend to move as expeditiously as possible to try to get you out of here in a reasonable length of time and to prevent you from becoming totally bored.

We had hoped to adjourn by 4:30. We will not meet that deadline, but we will move as expeditiously as we can.

I would strongly recommend that whenever a witness has submitted written material, that you simply ask to have that testimony put in the record, and you simply discuss the high points.

PANEL CONSISTING OF TAYLOR DAY, ROBERTO RUIZ, LONNIE GRAY, AND MARTIN ALVAREZ

Mr. MITCHELL. Leadoff witnesses for this afternoon are 8(a) firms—Mr. Taylor Day, president, Day's Cleaning Service; Mr. Roberto Ruiz, president of Maya Construction Co.; Mr. Lonnie Gray, president of United Guard Security, Inc.; and Mr. Martin Alvarez, president, Sun Eagle Corp.

If those four persons are present, will you please come forward to the witness stand.

Gentlemen, it is entirely up to you who will be the leadoff witness. As you can see, this is a very democratically run committee. We do not dictate here. You make the decision.

TESTIMONY OF TAYLOR R. DAY, PRESIDENT, DAY'S CLEANING SERVICE, TUCSON, ARIZ.

Mr. DAY. Congressman Mitchell, Mr. Hatcher, members of the committee, my name is Taylor R. Day. I am president of Day's Cleaning Service, located in Tucson, Ariz. I am very pleased to have been invited to testify before this committee and to be given the opportunity to comment on the current programs which assist small and disadvantaged business firms.

As a participant in the Small Business Administration 8(a) program, I am especially interested in directing my comments to the program. Before doing so, I would like to tell you more about my firm and its business activity.

I started Day's Cleaning Service in 1971 after serving 22 years in the U.S. Army. As a newly formed business, I soon became aware of the problems associated with being a small and minority owned firm.

My first few years of operation consisted mainly of small residential and commercial accounts. I was unable to pursue larger accounts, due primarily to the lack of financial resources and adequate equipment.

In 1972 I made application to the Small Business Administration for participation and was subsequently approved. My first 8(a) contract was awarded in 1972 and amounted to $12,000 a year providing janitorial services for the FAA in Phoenix.

In 1974, recognizing the need to diversify my business, I expanded our scope of services. During my first years on the 8(a) program, the overall 8(a) contract support was extremely limited. In 1976 I was offered the services of mess attendant at Luke Air Force Base and have done so to this date. Currently, I am only performing on one 8(a) contract and have not performed a janitorial 8(a) contract since 1976.

I would like to direct myself to a number of concerns which affect not only my firm, but other small and minority firms as well.

My first concern is the 8(a) program itself. Although it appears that my firm has been an active participant for 8 years, the length of time that I have been certified versus the amount of 8(a) project performed is very misleading.

With the exception of the last few years, the level of 8(a) contract support has been minimal in relation to other non-8(a) contract support. Just when it seems that a new emphasis has been placed on truly trying to assist firms such as mine, I find that the SBA is proposing that all 8(a) service firms be graduated or terminated within a 3-year period.

I am, of course, referring to the proposed rules which require SBA to establish a fixed period of time for every participant concerned to remain in the program. In reviewing these rules, I have yet to understand how the SBA made their determination regarding the maximum term of graduation for service firms.

It appears that the 3-year term was just randomly selected without any consideration of all factors which serve to make a firm viable and competitive. I would submit to this committee that the utilization of a fixed period of time criteria for participation on the 8(a) program would only service to fulfill the requirements of SBA and does little to assure that a firm is ready to compete in the open market once it is off of the program.

It would seem to me that SBA would want to consider other factors which would standardize criteria for determining the participation term for 8(a) contractors. Such factors would include but not be limited to financial capacity, management ability, and marketing capabilities. This would enable SBA to effectively monitor the progress of a firm on the program and determine when a firm is best suited to be graduated.

I firmly believe that graduation is a part of the 8(a) program and that each firm currently on the program must make every effort within their resources to become viable and competitive.

A second area which I would like to direct myself relates to Public Law 95-507 and the section dealing with subcontracting plans. I strongly feel that the subcontracting provisions which require prime contractors to submit, before the award of a contract, a subcontracting plan setting forth percentage goals for utilizing small and minority business should be fully monitored to insure compliance and enforcement.

As it presently stands, there appears to be a need to put some teeth into this law to get things done. I would also suggest that greater efforts be exerted by the governmental agencies involved, as well as the prime contractors to provide adequate notice of contracting opportunities to small and minority business concerns.

A final area of concern relates to the need for better access to information concerning opportunities for Federal contracting. While many of us request placement on bidders' mailing lists and subscribe to Commerce Business Daily, I still feel that there is something lacking.

Perhaps an expansion of the PASS—procurement automated source system—utilized by the SBA could be developed to provide small and minority firms with an accurate listing of Government contracting opportunities. Such a system, if expanded, could be very beneficial in providing such information as to the type of contracts available and the necessary resources and requirements needed to perform such projects. This would be very valuable and would serve as a tool for marketing with the Federal Government.

In conclusion, I would like to express my appreciation to all of the members of this committee for your interest and support of the small and minority businessperson. Thank you for providing me with this opportunity to express my concerns.

Mr. MITCHELL. We thank you for coming before the committee.

Congressman Hatcher, unless you object, I would like to get all of the testimony in, and then we will ask questions.

Our next witness.

TESTIMONY OF LONNIE GRAY, PRESIDENT, UNITED GUARD SECURITY, INC.

Mr. GRAY. I am Lonnie Gray. I would like to welcome you to Arizona and thank you for the opportunity to appear before this committee.

I am an 8(a) contractor in the guard service business, and I have participated in the program since June 1975, a total of 6 years. Let me assure you that the success of my firm depends not only on 8(a) but also on other factors in our local economy, which I would like to discuss this afternoon.

With respect to the 8(a) program, I am opposed to the proposed SBA rule which would limit program participation to 3 years for service businesses. The length of program participation should be dependent on the progress my firm makes to reach a competitive status in my market area. Participation should not depend upon an arbitrarily fixed date.

A review of my firm's level of participation in the 8(a) program over this last 6-year period will serve to illustrate my point. In 1975 my firm received 8(a) contracts totaling $56,210. In 1976 I only received $53,039, and in 1977 $50,195. Therefore, during my first 3 years in the program I received a total of $159,444, or a yearly average of $53,148. Since I generally operate on a 10-percent profit margin, this volume of activity represents a mere profit of approximately $5,300 per year.

If the proposed regulations were in effect when I first entered the program, I would have been terminated without any chance of survival at all.

After the initial 3-year period, however, our capacity to perform larger jobs increased, as well as our acceptance by SBA and buying activities of the Federal Government. In 1978 we received $94,267 in 8(a) contract awards, in 1979, $86,453 and in 1980, $246,992. Therefore, over our most recent history we have received $427,802 in 8(a) awards for a yearly average of $142,600. But our profit on this increased volume still remained at about 10 percent, or an average of $14,260 per year. As can be seen, we are moving toward becoming more competitive, but progress is extremely slow.

The 8(a) program was intended to correct the disadvantages suffered by people because of ethnic and racial discrimination. However, the ideals expressed by the Congress have not yet been realized. Nor will those ideals be furthered by a fixed 3-year participation which has absolutely no basis in logic.

My firm is the only black-owned security guard contractor in the State of Arizona. I can state without hesitation that 3 years is totally insufficient to achieve a competitive position in this market.

The SBA must provide me with the resources I need to become competitive. In essence, the length of my participation in the program is in great measure dependent upon how much help the Agency gives me.

I have made every effort to obtain Federal contracts outside of the 8(a) program. However, I have found it nearly impossible to get Government agencies to send me bid packages on their jobs, especially the Army bases.

Without the 8(a) program—despite the relatively small amount of contracts awarded during my first 3 years of participation—I would not have been able to survive.

I must admit that what I have heard and read with respect to this administration's position on SBA and the 8(a) program has caused me much concern. The effects can be devastating for this State, which has better than a 30-percent minority population. It is vital to the economic well being of Arizona that minority businesses be encouraged to grow and prosper.

I have spent most of my life in Arizona. I moved here in 1928. I expect to be allowed to participate in this growth unless the Federal Government sees fit to turn the clock back more than 20 years.

I must make the record very clear. Without a well-managed 8(a) program, one that develops firms to be profitmaking rather than concentrating on a fixed time of participation, the disadvantaged and minority segments of our communities all across the State and country will have no place to turn.

My experience of the past 20 years demonstrates that turning to State government for help will be of no value. Over this time I have found that approximately 80 percent of the State's security work has been given to a select few companies where I can find no bid process involved.

Cutting assistance to minority-owned firms, a willing employer of disadvantaged people, can have an extremely devastating effect.

I have noticed a significant number of persons have already lost their jobs because of Government budget restrictions. At the present time, I am plagued by applications from persons who live in disadvantaged areas of our community. My office is located in one of those areas.

The Arizona State senators and representatives have not indicated any willingness to adopt a State affirmative action program for minority-owned firms. Remarks by county and city officials indicate that they are only interested in dealing with big businesses with high dollar volume types of contracts.

We, as minorities, have been told that we will have to deal with our State legislature to take up the slack caused by Federal budget cuts. I, as many other minorities, deplore this type of approach which has caused much disruption in the planning ability of small minority-owned firms.

Federal assistance should be increased and should be better managed, and the States should complement this effort and not be held out as a total substitute.

We ask your support and commitment to insure a strong and viable SBA with the 8(a) program totally intact and operating in the way that Congress intended it to operate. Give the program the manpower which is very much needed to identify and negotiate contracts—to create jobs for the unemployed.

I have read Public Law 95-507 and so far, for Arizona, it is like reading a fairy tale out of a first grade reader.

This program can work if it is put on a sound business development basis. You must help to correct the shortcomings of the Federal bureaucracy. If you don't do this, the blame for this program not achieving its intended purpose will lie as much with the Congress as with anyone else.

Mr. Chairman, that concludes my testimony. I will be happy to answer any questions you may have at this time.

Mr. MITCHELL. Thank you. I do have some questions.

Just before we get to the next witness, I was under the impression that there was a State minority business development agency. Is there such an entity in this State, in the Governor's office?

Mr. GRAY. I think they have started to create something of this nature, but there hasn't been an impact as far as my business is concerned.

Mr. MITCHELL. I just want to know whether I am wrong. Is there such an entity now in operation?

OK. I am sorry. I am mistaken, then.

Our next witness.

TESTIMONY OF MARTIN ALVAREZ, PRESIDENT, SUN EAGLE CORP., TEMPE, ARIZ.

Mr. ALVAREZ. Mr. Chairman, I am Martin Alvarez. I am president of Sun Eagle Corp. We are an 8(a) firm and have been on the program since 1978. I will summarize my comments.

Since our firm is a construction company, most of the comments that I will be making will be in respect to the Small Business Administration's evaluation of construction companies on the 8(a) program.

The proposed change would limit the life of the 8(a) program for a construction company to 5 years. As has been stated previously by others, that in reality poses a great deal of problems in that you cannot evaluate a conventional business in America on a timeframe.

You would have to evaluate it, in my opinion, by evaluating the components that make the company a viable entity, and a viable entity, in my mind, especially in terms of a construction company, has the following ingredients.

I think in the event that the SBA is seriously going to consider evaluating firms and seriously trying to create viable firms in the future, they are going to have to evaluate them in the following manner, especially, as I said before, construction companies.

No. 1, they have to evaluate the bonding capacity of the firm. It is a subjective method of evaluating a firm, and it will give you the insight into the capacity of the firm from day 1 and 5 years later, 3 years later, whatever the amount of time.

If a firm, let's say a general contracting firm, does not have bonding capacity, their likelihood of survival in the conventional market is zero. So, this would have to be one of the major criteria that SBA would have to employ in evaluating the firm.

In the event that the firm needs assistance, the SBA has a guarantee program for the bonding which can run parallel with the 8(a) program, which is ideal.

The second area of critique on the firm would have to be the financial capacity of the firm: The ability of the firm to borrow in the short term; the ability of the firm to borrow in the long term; and the sources of this type of financing.

Critical for construction companies is their ability to borrow in the short term. No 1, they have to be able to borrow short-term money even if they have to pay 22 percent for it.

Whatever the case may be, and in order to capitalize the firm down the road, they are going to have to acquire equipment, and most construction firms will have to deal with financial institutions of various sorts to borrow money for equipment.

The third area is the equipment and the facilities. When entering the 8(a) program, the SBA has to evaluate the equipment and the facilities of the firm.

Second, as the firm progresses from year to year, or 18-month basis, or whatever evaluation period SBA would choose, the new equipment that has been acquired, the debt service on that equipment would have to be evaluated.

When that is made part of the 8(a) program, when the SBA can evaluate the type of equipment that the firm has, the quality of the equipment, and the debt service, then they can say whether or not this firm can be a viable firm.

Without that equipment, or without access to that equipment, or access to financing, it is almost impossible to create a viable firm. You will create a firm which is dependent on financing from one job to another, and you really won't create anything but havoc.

The fourth area is the area of management. The SBA should have to evaluate the competence of the management of the firm. When they evaluate the owner, they should also evaluate the key people in the firm, such as the estimators; the CPA's that are doing the external work; the internal accounting people; and whatever other key people are in the firm: the personnel people, the superintendents, and so on.

The last area is the marketing expertise that the firm should employ if it is going to survive in the long run. The SBA can easily create a quantifiable vehicle to evaluate the marketing expertise of a firm. If they know how to bid in various segments of the market, if they can do Federal, State, city, private and whatever other types of work there are, and if they can diversify their firm, and have the ability to bid and to learn, then they have achieved the marketing element of my proposal.

In the final analysis, the SBA would evaluate all five key areas and graduate those firms who have achieved success in all of the areas. It may take 3 years for some firms. It may take 5 for others. It may take longer for others.

But to place a time constraint on an 8(a) firm is totally out of context with everything else that you have in American business.

Thank you, sir.

[Mr. Alvarez' prepared statement follows:]

PREPARED STATEMENT OF MARTIN ALVAREZ, PRESIDENT, SUN EAGLE CORP., TEMPE, ARIZ.

The U.S. Small Business Administration has recently proposed changes to the 8(a) Program which will have a significant effect on all 8(a) firms throughout the United States. Sun Eagle Corporation, in the following testimony, wishes to comment on the proposed changes. Sun Eagle Corporation has been on the 8(a) Program since August 10, 1978.

It is our understanding that the new proposed rules would limit service firms to three years and construction, manufacturing, and other firms to five years on the program. We understand the government's position in identifying a time frame for the 8(a) firms. We, however, disagree with a fixed time rationale for graduation. This method of graduating 8(a) participants is unfair to those firms whether service or construction oriented who are not managerially improved due to the inability of the SBA to secure ample work for the firm in question.

We, hereby, propose a more subjective method of evaluation for 8(a) firms. Our management proposal and evaluation process would be segregated in five different areas of evaluation. These areas are:

(1) Bonding Capacity;
(2) Financial Capacity (Revolving Lines of Credit and Ability to Borrow Money in the Short and Long Run);
(3) Equipment and Facilities;
(4) Management, Expertise;
(5) Marketing, Expertise.

We propose that the Small Business Administration use these five criteria as a management tool for evaluating progress and ultimately for determining a graduation date from the 8(a) Program. Criteria should be determined by industry and more specifically by trade or type of business within the industry.

(1) BONDING CAPACITY

Construction companies most generally are evaluated and progress according to their ability to bond projects in the market place. All 8(a) projects exceeding $25,000 require a Performance and Payment Bond. Likewise, most all major private or public works projects require bonding by the prime contractor. In order to effectively compete in the market, it is necessary to have a bonding line of credit which will allow the contractor the flexibility to bid projects in his own area of expertise and of the size which will effectively allow the company to grow progressively from year to year.

It should be the responsibility of the agency (SBA) to assist in expanding the bonding line of credit. As a firm has more flexibility, it can avail itself to numerous projects on its bidding schedule in a year's time. It should be understood that construction firms generally win 10 percent of the projects they bid in the competitive market, that is, a firm starts on the 8(a) Program with a $100,000 bonding capacity and at the end of five years has increased its capacity to $200,000 and simultaneously graduated from the program, it cannot be concluded that this firm is viable as a result of this single indicator. Although progress has been made, the firm may still be incapable of competing in the market place without further assistance. Due to the other factors which play a significant role in determining overall success of the firm.

The viability of a firm cannot be determined unless a complete management evaluation is made which includes evaluating the bonding capacity along with the other critical elements which follow.

(2) FINANCIAL CAPACITY (REVOLVING LINES OF CREDIT AND ABILITY TO BORROW MONEY IN THE SHORT AND LONG RUN)

As an integral part of a management evaluation, financing is one of the primary components in evaluating the success of a firm. Financial capacity for construction firms is generally associated with their ability to borrow short term money to finance projects and long term money to finance major equipment. An evaluation must be made of all 8(a) firms which evolves around those companies ability to borrow in the short and long run. The ratio between firm's gross sales and its ability to borrow on a line of credit basis can generally determine the financial stability, leverage, and ultimately the success of those firms. That is: If a firm has a revolving line of credit with a commercial bank for $20,000, most generally it is assumed that the maximum gross sales capacity of the firm is $200,000. This ratio can be altered depending on the internal cash flow of the firm. The internal cash flow is generally determined by the nature of the work and by the clients of the firm. Most generally it is an industry norm that a line of credit for 10 percent of the gross volume will effectively finance sales for that firm.

The Small Business Administration should evaluate the line of credit and its future potential for increases with the type of firm. It can effectively determine the internal cash flow of the company since the Small Business Administration is already receiving quarterly financial statements from its 8(a) clients. Upon determining the ideal line of credit, the agency can further determine the ability of the firm to effectively compete in its segment of the market.

Long term financing for capital equipment expenditures is vitally important to construction companies. If a company has the capability of borrowing in this area, it can effectively acquire the proper equipment necessary to compete with other firms utilizing the same or similar equipment.

The agency should evaluate the short term and long term financial capacity of the 8(a) company and correlate their evaluation with the industry norm for similar firms.

(3) EQUIPMENT FACILITIES

Construction companies are extremely dependent on equipment in competing on projects. Viable and competent companies charge their equipment to specific jobs by using a formula which is consistent with their lease payment or debt service payment. If 8(a) firms are to survive as viable entities, they must effectively acquire equipment and charge it proportionally in order to remain competitive. The initial acquisition of this equipment is the critical determining factor in the success or failure of new construction firms. If a firm acquires too much debt service for its equipment purchases, it is then saddled with the necessity to acquire projects in order to service the debt.

The 8(a) firms, in many cases, are not readily extended credit for the acquisition of equipment. Generally, major equipment is financed through different sources from commercial banks. These companies who specialize in equipment financing require different criteria from their clients. The 8(a) clients who need major equipment for the success of their firm must not allow themselves to guarantee accounts receivable and equipment because they may lose their overall leverage which must be planned in order to retain their short term borrowing capacity.

(4) MANAGEMENT EXPERTISE

Prior to being graduated under the 8(a) Program, clients should have retained enough solvency to have acquired management talent such as a CPA firm and a law firm in an advisory capacity. The client should not be graduated until he also can hire employees who are capable of complementing their firms with expertise in critical areas. Construction companies need engineering and estimating talent, financial and management talent and field and supervisory talent. With the acquisition of this type of management expertise, 8(a) firms are more apt to remain viable and survive in the long run. In the construction industry nearly all projects are competitively bid. It is the responsibility of each firm to upgrade new techniques involved in conventional construction and new uses of equipment and personnel. These innovations help upgrade the industry and likewise help the more competitive firms survive the cyclical nature of the industry.

As companies become larger, they learn to become more efficient in their bidding procedures, thus, allowing them to bid hundreds of projects per year. This shotgun approach to bidding projects is often similar to the same marketing techniques utilized by advertising firms implementing mail order letters, cards, and games for retail sales. If these types of techniques are being successfully implemented by construction companies, then 8(a) firms as competitors, must use these techniques or develop more innovative techniques of their own, if they are to survive.

(5) MARKETING EXPERTISE

The 8(a) firms like any other companies must have a marketing program which will allow them the latitude to win projects in different segments of the market. Those firms specialized in performing only one segment of the market on many occasions do not survive short term depressions in the market. With a competent marketing plan, 8(a) firms can achieve a balance of construction projects which will include government work, commercial work, and private work. When 8(a) firms are able to mix their level of work, then they can achieve the competitive status they want to attain.

As the Small Business Administration develops criteria for each industry in which 8(a) firms are engaged, the agency can readily determine the level of competitiveness by virtue of the easily comparative data it establishes.

Should you have any questions regarding our testimony, please feel free to call us at the number provided.

Mr. MITCHELL. Thank you.

Mr. Ruiz, please.

TESTIMONY OF ROBERTO RUIZ, PRESIDENT, MAYA CONSTRUCTION CO.

Mr. RUIZ. Mr. Chairman, Mr. Hatcher, members of the committee, my name is Roberto Ruiz. I am president of Maya Construction Co.

I would like to read my statement. It is brief. It will indicate the success or the help that the 8(a) program is providing my company.

I have some recommendations as to what can be done instead of the regulations that are being proposed by the SBA office.

I just want to say I am extremely honored to have been invited to testify before this committee, and I am very encouraged to see that your Committee on Small Business is interested in improving Federal programs so as to help small and disadvantaged businesses overcome impediments to their development.

Let me assure you that there are many impediments in this regard.

Prior to sharing with you some of my thoughts regarding these programs and giving you my impressions of areas of concern, I would like to give you a little background on the firm.

Maya Construction Co. was established by myself in 1977 and is licensed by the State registrar of contractors to provide general contracting and engineering services. Although the firm was incorporated in 1977, we did not undertake construction activity until January 1979.

In June 1978 our firm filed an application with the Small Business Administration for participation in the 8(a) program and this application was subsequently approved in September 1978. We did not perform on our first 8(a) contract until July 1979.

During our first full year of operation in 1980 our firm achieved $670,000 in sales, of which 39 percent were 8(a) related and 61 percent were non-8(a). In our present fiscal year we anticipate annual sales in excess of over $1 million, which presently consist of 55 percent 8(a) contracts and 45 percent non-8(a) contracts.

Although certified for the 8(a) program, our first 1½ years of overall construction activity could be best summarized as follows:

Due to our newness and lack of track record, we were unable to secure adequate financial and bonding support. As a result, we were required to undertake small projects which required limited capital resources and little or no bonding.

Bonding which was available in a limited amount was secured by a 90-percent guarantee offered by the SBA surety program. Likewise, financing for projects was based upon the assignment of contracts, as well as all other business and personal assets, which included my home and the kitchen sink.

Projects made available through the 8(a) program were normally small in nature and generally related to construction remodeling.

Finally, the number of projects made available under the 8(a) program were very few in number.

During the past year our firm has experienced a considerable, positive change in some of the obstacles previously encountered. Much of this is directly attributable to the benefits derived from the 8(a) program, and to the strong support given the program by the SBA District Office and the Director, Mr. Tom Trimboli.

With his support, both of the offices' business development specialists, Mr. Mike Enriquez and Mr. Wilfort Hankins, have undertaken an aggressive effort to make the program more effective and beneficial to all parties concerned.

One of the major concerns affecting the 8(a) firms in this State is the proposed amendments to the current regulations requiring SBA to establish a fixed period of time for every participant concerned to remain in the program.

Although I feel that it is essential that graduation be a part of the 8(a) program, and I recognize the desires of the SBA to deal with this issue, I feel that the fixed program participation term as defined in the proposed rules does not meet all the concerns associated with the intent of the program, and the intent of the program is for firms to become a viable contractor.

In other words, the proposed rules, while dealing with the questions of how to get firms off the program gives little attention to the individual firm's ability to achieve viability, which is what the program is all about.

Rather than being critical of the new rules, I would like to suggest that more objectivity be utilized in determining a firm's graduation from the 8(a) program, rather than utilizing a fixed period of participation, which does not consider all the factors which impact on the viability of a business.

Recently, our firm was selected to voluntarily participate in a demonstration project being proposed by the Phoenix district SBA office as a means of monitoring the progress and development of 8(a) firms. Under this test project, our firm was reviewed and evaluated in a number of areas, including finance, marketing, and management.

Within each element of the review process of the 8(a) firms utilized by SBA district office, various key indicators were established to help track and monitor the progress of each firm.

For example, in the area of finance, key financial ratios—such as net profit to sales, quick ratio, debt to worth ratio, fixed assets to net worth and sales to working capital—were utilized to determine the firm's financial position in relation to the best available norms of related industries. This evaluation serves to enable the SBA to determine how each firm is progressing toward achieving financial viability.

In the area of marketing, each firm is to be evaluated in a key number of areas including sales trends, percentage of non-8(a) sales of total sales and overall marketing efforts such as identification and segmentation of the market, effectiveness of bidding efforts in the non-8(a) marketplace, advertising methods and resources, pricing considerations and strategies, public relations, budget planning and analysis and review of marketing efforts.

In the areas of management, each firm is to be reviewed on the basis of its overall planning efforts in developing a comprehensive business plan, the firm's organization, staffing and control, and the firm's review of its management efforts with the necessary feedback to improve operations.

This type of evaluation is to be performed on each 8(a) firm on a quarterly basis with the results documented and discussed with the 8(a) client.

I would strongly urge that this type of business analysis and evaluation be considered as a model for monitoring the progress of 8(a) firms and as a means for establishing quantifiable graduation criteria, as opposed to a fixed termination period based upon a prescribed number of years.

Not only does this serve as an evaluation guide for the SBA, but it also serves as a key business barometer for the 8(a) firm. This, coupled with other 8(a) requirements, such as the development of annual business plan updates, enables the individual 8(a) firm to adequately plan its development and progress toward achieving viability.

Within the construction industry, there are two additional areas which must be considered in determining, whether or not a firm is considered viable, and thus able to compete in the open market. These areas relate to bonding and the acquisition of fixed assets.

In the bonding area it is extremely critical that a firm be able to establish a solid financial position, as well as a track record for successfully completing projects, if it is to build its bonding capacity.

In the construction industry, bondability is an essential element of competitiveness. Without it, a firm cannot openly compete for large public and private projects. Therefore, it is essential that SBA consider where a firm stands in relation to bonding capacity as an element of determining graduation.

As with bonding, the acquisition of fixed assets is also critical in the construction industry. If a firm is to compete in the open market, it must have the resources to acquire the needed equipment and facilities. Without it, a firm cannot openly compete for large public and private projects. Therefore, it is essential that SBA consider where a firm stands in relation to bonding capacity as an element for determining graduation.

As with bonding, the acquisition of fixed assets is also critical in the construction industry. If a firm is to compete in the open market, it must have the resources to acquire the needed equipment and facilities. Without it, a firm will not be able to compete with firms that do have the financial resources to acquire equipment.

I would again urge that this be a factor of consideration in determining the graduation of a firm from the 8(a) program. At this time, I also would like to mention that it is essential that the SBA continue to provide business development expense funds in order to assist those firms who need to acquire equipment but do not have the available financial resources to do so.

In many instances, the acquisition of equipment through the use of BDE is the only alternative available to the 8(a) contractor, who cannot use precious working capital funds for fear of extending the firm to the point of affecting bondability and ultimately the ability to compete for contracts.

In conclusion, I would like to state that the 8(a) program has been very helpful in assisting in the development and growth of my firm. Certainly without the program my firm could not have been able to make the kind of progress that it has to date. I would urge that the 8(a) program be continued and improved as required.

Finally, I would like to commend this committee and particularly each of the members present for taking the time to visit our State and to give individuals such as myself the opportunity to participate in a process designed to assist the small and disadvantaged businessperson.

Thank you.

Mr. Mitchell. Thank you very much for excellent testimony.

Congressman Hatcher, do you want to lead off with questions?

Mr. Hatcher. Thank you, Mr. Chairman.

Mr. Day, you and the others seem to favor graduation of 8(a) firms at some point. Yet, everyone seems to be concerned about putting a 3-year or 5-year limit. Do you think any timeframe can be acceptable? Do you think every 8(a) firm should at some point graduate?

Mr. Day. Yes; I do at some point. However, large firms, if you check, you will find that it takes anywhere from 10 to 12, 15, and in some cases as high as 20 years before they are able to be viable and competitive.

I do not understand how anyone can think that a small firm can be competitive, viable, in 3 to 5 years.

Mr. Hatcher. Or that every firm could be expected to do that.

Mr. Day. If they expect a small firm to do it, I suspect they expect everyone to do it. It is just an impossibility, as far as I am concerned, for any organization, any business to be competitive or viable in 3 to 5 years.

Mr. Hatcher. You think it is possible to put a timeframe on graduation, or you think it has to be left up to the individual company?

Mr. Day. Sir, I don't agree with a timeframe at all. I think what you need to do is monitor—as I stated in my statement, I think each individual business or organization should be monitored, and when they feel they are viable and competitive, that is when they should graduate, not 3 years, not 5 years.

I don't agree with anyone that suggests something like that.

Mr. **Hatcher**. What if it is 25 years? Do you think you should continually give some sort of benefit to a firm which, for example, after 25 years has not found a way to compete?

Mr. **Day**. Not 25 years, but I still don't think there should be a time limit. I don't agree with that.

Mr. **Hatcher**. Thank you.

That is all, Mr. Chairman.

Mr. **Mitchell**. This has really been just fascinating for me. Congressman Hatcher, I would like to put this on film and play it for the whole committee. Here you have people who have been working at this. They have come up with intelligent and reasonable criteria for graduation. It is just fascinating. I want to dig into that just a little bit more.

First of all, for all four witnesses, what percent of your business is 8(a) and non-8(a) at the present time?

Mr. **Ruiz**. At the present time, Mr. Chairman, the percentage of 8(a) contracts is around 55 percent and non-8(a) 45 percent.

Mr. **Mitchell**. And yours?

Mr. **Alvarez**. Around 50-50.

Mr. **Gray**. Mine is about 45 percent 8(a) and 55 percent non-8(a).

Mr. **Day**. About 60-40; 60 percent 8(a) and non-8(a) 40.

Mr. **Mitchell**. That is the kind of mix I think we would like to see companies develop after 3, 4, 5 years. I think after you begin developing that kind of mix, you are well on the way to becoming a viable company.

Mr. Ruiz, that is an excellent demonstration project that you talked about. That came through the Phoenix district office?

Mr. **Ruiz**. Yes; that is correct.

Mr. **Mitchell**. It is now in operation?

Mr. **Ruiz**. It is a test program. It has been submitted by the district office to the region. Right now the region has submitted it, as I understand it, to the Washington offices.

Mr. **Mitchell**. You know, I think it is just excellent, but I have a larger question. Why the devil wasn't this being done all the time, since the beginning of the SBA program? Why didn't somebody have the sense and gumption enough to set forth some specific stages of development so that you are able to say at the end of this quarter we know where this company is, at the end of the half we know where this company is.

It is always OK to argue this as hindsight, but it just seems to me that should have been the function of the SBA from its very inception, to set up specific goals, specific criteria, and to monitor them on a quarterly basis.

I know what the answer of SBA is going to be—they don't have the personnel to do that. But to that I respond had you come here and made out a case in past years for this kind of really intensive followthrough, I think the Congress would have been responsive. I honestly do. It might be a little more difficult right now.

How many people do you employ? I know it is kind of seasonal, but on the average during the course of the year.

Mr. RUIZ. Well, Congressman Mitchell, at the present time I have eight people working. I am in the process of hiring about six or eight other people, because we have not started to perform on a million dollar contract.

Mr. MITCHELL. All right. Then on the average you are talking about maybe 12 people per year?

Mr. RUIZ. I would say so.

Mr. MITCHELL. Mr. Alvarez, on the average?

Mr. ALVAREZ. On the average about seven people.

Mr. GRAY. Between 60 and 85.

Mr. MITCHELL. Sixty and eighty-five during the course of a year?

Mr. GRAY. Yes; in the course of a month.

Mr. DAY. About 175.

Mr. MITCHELL. On the average during the course of a year?

Mr. DAY. Yes, sir.

Mr. MITCHELL. And you are about equally mixed in terms of your 8(a) and non-8(a)?

Mr. DAY. Right?

Mr. MITCHELL. In the event that the Small Business Administration—I started to say arbitrarily but that is not a good word, nor is capriciously—summarily decided to drop you from 8(a) status, how many of your present employees would you be able to retain?

Mr. GRAY. Less than 50 percent.

Mr. DAY. More than 50 for me. One 8(a) contract has 67 people. The only contract I have has 67 people. It would be about 40 percent.

Mr. ALVAREZ. 50 percent.

Mr. RUIZ. I would say 50 percent.

Mr. MITCHELL. I guess that is kind of a signal that I would like to send to the Small Business Administration, that if you want to make changes, fine, but don't make those changes precipitously without measuring the impact in terms of employment of people in small business, and a whole host of other criteria.

Mr. Alvarez, you warm the cockles of my heart in setting forth your very excellent recommendations for criteria for evaluation of 8(a) firms. It was just excellent.

Mr. ALVAREZ. Thank you.

Mr. MITCHELL. I am personally going to see that the Administrator gets this. It is a sensible, rational way of approaching this problem, rather than saying 3 to 5 years, or 18 months or 10 years. It is a logical, sensible way of doing it. I am really very, very delighted about this.

On the bond problem, there is a limitation of $100,000 imposed by SBA for certain bond waivers. Is that $100,000 sufficient?

Mr. RUIZ. No; it is not.

Mr. MITCHELL. Why not?

Mr. RUIZ. Right now, I have a bonding limit of approximately $2.5 million.

Mr. MITCHELL. $2.5 million?

Mr. RUIZ. Yes. That would not begin to touch it.

Mr. MITCHELL. What about you? Is $100,000 adequate?

Mr. ALVAREZ. No. Our bonding capacity is about $1.5 million. The projects we are bidding on are in the neighborhood of $700,000 or $800,000 a job. So for us it is not feasible to use the program because to do a job of that size and to get a 90-percent guarantee from SBA and wade through the paperwork you have to do, you would never have time to bid the job. You have a leeway of about 2 weeks to bid a job. Although the program is good——

Mr. MITCHELL. It doesn't move fast enough?

Mr. ALVAREZ. There are problems that the program inherently has. It probably is good for somebody who is on an 8(a) or on a particular project where you have a lead time, but it may not necessarily be a functional type of program for somebody who is bidding work all the time.

In our case, we probably bid on 74 jobs in the last 9 months, and won maybe 3. So you don't have a lot of time to spend running down paperwork. You just have to bid them as they come.

Mr. RUIZ. Mr. Chairman, I was in the SBA warranty bonding program. It would take anywhere from 2 to 4 weeks to get my bonding. It would just shove me out of the saddle as far as considering any projects.

The bonding company that I was dealing with was telling me, "As soon as we can, we will get you off of the program," because it is just not the way to go.

Mr. MITCHELL. Enlighten me a little bit in terms of contract work. You make your bid. You need your bond—48 hours, 72 hours. What kind of timeframe are we operating on?

Mr. RUIZ. First of all, you have to submit a bid bond with it. At that time you would have to guarantee that you would have a bond. Under the guarantee, SBA guaranteed bonding, they would not do that.

Mr. MITCHELL. No. But forget the SBA program. What is the timeframe that you would need in operating outside of SBA?

Mr. RUIZ. I would say within, at the most, 10 days, and sometimes they do require it within 3 or 4 days.

Mr. MITCHELL. OK. I just have a couple more questions. You can see that your testimony is fascinating to me. These questions are directed primarily to Mr. Day, and also to Mr. Gray.

Both of you refer to the difficulties that you have experienced in receiving bid packages from the Army and other agencies. I would like for you to elaborate a little bit on that. Let me tell you why.

It is my understanding that the Small Business Administration is in contact with the local agencies. It should get a listing, it seems to me, of bid packages almost as quickly as they are prepared by the military.

Then I would assume that the SBA would get those packages out to interested parties. Apparently that is not the way it is working. You tell me what the problems are, how it has worked, and what you would recommend to resolve this particular problem.

Mr. DAY. Well, in my particular case I have been getting them by going on a bid list. I call or even go in some cases and pick up the form, fill the form out, and turn it in. There have been many cases, especially with Fort Huachuca where I am on the bid list, but I never get a copy of the bid.

Each year when the bid goes out, or 2 years, when it is out for bid on the street—and I don't receive a copy of it, I called and asked them, and they said, "We only have 15 to send out this year." I said, "I have been on the bid list 4 or 5 years, why don't you send me one."

This year they sent me one, but there is a bond requirement on it. It is almost an impossibility for a janitorial company to get a bond. A bid bond you can get anywhere. It is for the performance bond the problem comes in. It is not like a construction company. Bonding companies don't like to deal with janitorial companies. When they find you put a lot of pressure on them, they put the bond on.

I expected when I got the contract this year there was going to be a bond because 3 years ago I wrote a letter to GAO, and I had an investigation at Fort Huachuca. Ever since then I never had another chance to bid until this year, then they put the bond requirement on it, knowing I could not get a bond requirement for a $750,000 contract.

Mr. MITCHELL. At some time in the future would you send me in writing why you asked for the investigation. I won't ask you to do that today.

Mr. DAY. I can send you the GAO report, the whole thing.

Mr. MITCHELL. Thank you.

Now, Mr. Gray, in terms of your attempts to get some bid packages.

Mr. GRAY. Each time Fort Huachuca has put out a bid package it always ends up SBA trying to get assistance through them, to get a copy of the bid bond. By the time I get a copy of the bid bond and by the time I get the package together, the time limit is too short.

Mr. MITCHELL. What is generally the time limit?

Mr. GRAY. Three or four days before the closing of the bid. It is impossible for me to put a proper proposal together to send back to them, and to get the bonding that is required. I would like to also say, since we are talking about bonding, for me to bid with most of the firms here, I have to get a million dollar bond.

That is one of the eliminating factors that electrical firms use in this State to control what type of security they have. I have one firm that dropped to half a million, but the rest of them tell me $1 million.

I have to have the bond by the time I go to work with them. I tried Fort Huachuca and Yuma, also. I have been to Yuma dozens of times.

Mr. MITCHELL. To the best of your knowledge, is that same kind of requirement imposed on the larger security firms, the Pinkertons and so forth?

Mr. GRAY. What they do with those firms I have no way of knowing.

Mr. MITCHELL. That is an awfully high bond. I am aware of the sensitivity of materials they are working on.

Gentlemen, thank you very much. I have learned quite a bit.

Our next witness is Dr. Gloria Little, a member of the Arizona Federation of Business and Professional Women.

Dr. Little, thank you for being with us this afternoon.

TESTIMONY OF GLORIA LITTLE, PAST PRESIDENT, ARIZONA FEDERATION OF BUSINESS AND PROFESSIONAL WOMEN, AND PROFESSOR OF BUSINESS, SCOTTSDALE COMMUNITY COLLEGE

Ms. Little. Good afternoon.

Mr. Mitchell. Dr. Little, your testimony is relatively brief. You can read it in it entirety, or you can submit it for the record and merely refer to the highlights.

Ms. Little. I would like to read it entirely, if I may.

Before I begin my testimony, I would also like to call attention to the committee the handsome tie worn by the chairman, because I believe it came from a woman-owned business.

Mr. Mitchell. Indeed it did.

Ms. Little. I have tried to make my testimony mercifully short in deference to the committee and have attempted to address only those issues that have not been emphasized by previous witnesses.

I note that many of the previous testimonies were given by groups. I wonder if there is any significance to the fact that I sit here alone.

Mr. Mitchell. Yes, there is. It is the feeling of the Chair and the members of the committee that the women businesses must be stronger because they have survived. Therefore, you could come up alone.

Ms. Little. Thank you.

My testimony today will be made first from the viewpoint of local women who are or would like to be small business owners and second as a respresentative of the Maricopa County Community College district concerned with continuing education for potential and/or current small business owners, both men and women.

Like minority small business owners, women report three major areas where they lack access. They lack access to capital. They lack access to markets—specifically, Federal, State, and county contracts. They lack access to meaningful continuing management and technical assistance.

An adequate data base about women business owners is not available. Very little information about their personal characteristics, the characteristics of their businesses, their experiences as business owners, or their special problems has been systematically gathered.

Until the Department of Commerce published "Women-Owned Business 1972" in 1976, the number of women-owned businesses in the country was unknown. In 1972, according to the report, 4.6 percent of all firms were classified as women-owned. More startling, the gross sales receipts of these businesses represented 0.3 percent of all business receipts that year.

The Federal study revealed that 98 percent of these businesses were sole ownerships and that women-owned businesses tended to be concentrated in labor-intensive industries that require low capitalization and often show a low return on investment, such as beauty shops, secretarial firms, and small retail stores.

The Bureau of Census in 1977 reported that 702,000 businesses were owned by women and their receipts totaled $41.5 billion for the year. The largest number of businesses were classified as miscellaneous retail.

Women business owners are likely to play an increasingly vital economic role in the eighties, but more research must be conducted in order to effectively assist them. If Federal agencies and private industries are to become responsive to women's needs, comprehensive profile data on women business owners must be collected nationally and locally.

Women often encounter sex-related problems such as establishing credibility in predominately male fields and related difficulties in obtaining loans and establishing credit.

Several women interviewed locally reported that they felt their loan applications were unjustly scrutinized and evaluated more carefully and conservatively than necessary with the whole process unduly prolonged despite the 1975 Federal Equal Credit Opportunity Act which makes it illegal for lenders to discriminate on the basis of sex or marital status in considering credit and loan applications.

One business owner, a woman, described the process of applying for an SBA loan as overly bureaucratic with the paperwork frustrating and the waiting period for the loan to be processed unrealistic.

Local women also report difficulty establishing themselves in the informal network that makes Government contract information that is timely and accurately available to them. Subcontracting opportunities are also few and far between for women owners because of the gap in the personal and business contacts which exist for women who often are not members of the local chamber of commerce or of men's service clubs.

Women lack access to practical management and technical assistance. As a matter of fact, effective management and technical assistance is not readily available to men or women. An effort to provide appropriate short-term training to small business owners is evidenced by the 18-month contract awarded to the American Association of Community and Junior Colleges to develop a coordinated national network for small business training based on 163 2-year college campuses.

Scottsdale Community College, Rio Salado Community College, Navajo Community College, Northland Pioneer Community College, and Pima Community College are part of that national network committed to extending skills to the small business person in Arizona.

During the first 6 months of 1981 over 24,500 men and women participated in 757 high quality, short-term training activities cosponsored by the National Small Business Training Network institutions and the Small Business Administration.

In addition, over 60 institutions collaborated with financial institutions, such as banks and savings and loan associations, to deliver training targeted to veterans and minority groups.

Community colleges have taken the leadership to provide low cost, locally oriented, high quality instruction across the country. Community colleges are uniquely qualified to work successfully with local SBA district offices to increase outreach to women, minorities, and veterans, as well as traditional student populations.

The network has been invited by the Small Business Administration to submit a proposal for extension of the project from February 1, 1981 until December 31, 1982. I strongly urge the funding for this extension. The community colleges in Arizona and across the Nation can deliver the kind of management assistance that will make a measurable contribution to the economic health of the local community and of the Nation.

That concludes my testimony.

Mr. MITCHELL. We thank you for your testimony.

I think it is laudable that you got your academic institutions participating in this, doing this kind of endeavor. Have you ever run a business? Are you in business yourself?

Ms. LITTLE. Yes.

Mr. MITCHELL. What is the nature of your business?

Ms. LITTLE. Small consulting firm.

Mr. MITCHELL. Generally at the colleges that you have delineated in your testimony, are people involved in this project—people who have had some experience in running a small business?

Ms. LITTLE. Yes.

Mr. MITCHELL. That is excellent because one of the things that has irked me so badly in Government is to find people who never have run a business trying to give direction and make policy for those who have run businesses for years. It just doesn't make any sense. I feel just as strongly about somebody offering technical assistance who had not had the opportunity to run a small business, or to run any business at all.

One of the charges that we hear—last night in the presentation I said that the Federal Government's efforts on behalf of small business, minority business in particular, are just constantly maligned and discredited and so forth.

One of the things we have heard so often is insofar as minority businesses are concerned, 99—and I put that in quotes—99 percent of them are front companies. That is just not true.

The same charge has cropped up now with reference to women in business, women as minorities. I know that the Department of Transportation specified women as minorities administratively, and we immediately heard the charges the women are there in name only, they are fronting for males. You have heard those charges.

Ms. LITTLE. Yes.

Mr. MITCHELL. Do you have any data to refute those charges?

Ms. LITTLE. No; I do not.

Mr. MITCHELL. I think it would be enormously important for someone to start to collect that data as quickly as possible. We find when these spurious allegations are raised, if we have data right away, it is very beneficial. Maybe that would be a project this consortium of colleges could undertake.

Ms. LITTLE. Yes; lacking two important elements—time and money—for that research.

Mr. MITCHELL. Really it is a responsibility, I would assume of the Small Business Administration, since it is sponsoring this kind of effort.

As was true with one of the other witnesses earlier, I want to dig just a little bit into more specifics with reference to your testimony where you point out that for women—there is unjust scrutiny and evaluation made by banks on loan applications submitted by women. Could you be more specific?

You also talked about a prolonged, delayed time, a longer delay time in either approving or disapproving the loan.

Ms. Little. I wish I had statistics to back up this sort of thing, but the time that I had to prepare my testimony was very short; frankly, insufficient to gather the appropriate data. This came, frankly, from telephone conversations with businesswomen owners.

Mr. Mitchell. One last question. You indicated that, like some other minorities, you are not a part of the good old boy's club, whatever that means, that you don't have membership in the chamber of commerce, or you are not with other service groups that are primarily male.

Why is that true? Are women excluded by some sort of bylaws or is there voluntary exclusion on the part of the women themselves?

Ms. Little. Sometimes the exclusion is financial in nature. Sometimes it is a matter of time. The struggling woman business owner cannot afford to belong to some of these organizations. Also, she doesn't have the time to do that.

Mr. Mitchell. Then much of it is not an exclusion imposed on women. It is an exclusion based upon the time constraints and so forth.

Ms. Little. Yes.

Mr. Mitchell. Congressman Hatcher.

Mr. Hatcher. Thank you, Mr. Chairman.

Dr. Little, we often hear or read that women control the wealth in this country. Is that true?

Ms. Little. Do you expect an answer to that, Mr. Hatcher?

Mr. Hatcher. Well, I wondered from your last answer. If it is true, as I suspect it is, is it the women who are trying to get in business are not the women who have that money, maybe?

Ms. Little. Well, all major institutions in the United States are still controlled by men. Wouldn't you agree, Mr. Hatcher?

Mr. Hatcher. I would. I would like to ask you about the network—the good old boy club, rotary club, golf club. What can the Congress of the United States do to alleviate that problem, if it is a problem, for women trying to break into business?

Ms. Little. I don't have a specific answer to that. I am sorry.

Mr. Hatcher. Thank you.

Mr. Mitchell. Thank you very much. I guess I don't have an answer, either. My hunch is there is not very much we can do about it. Only in those situations where existing civil rights laws are applicable, maybe we can operate, but beyond that I don't know.

PANEL CONSISTING OF ROBERT DeBOW, JOHN HANSGEN, SR., E. DANSON PERIN, AND NATE COLLINS

Mr. Mitchell. Our next panel is a panel of banks—Mr. Nate Collins, vice president of corporate banking, Valley National Bank; Mr. John Hansgen, Sr., vice president, business loan group, Thunderbird Bank; Mr. E. Danson Perin, executive vice president of the Arizona Bank; and Mr. Robert DeBow, president, Copper State Bank.

Gentlemen, thank you very much for taking the time to stay with us all day. Again, I want to emphasize, I think it is important that we come out to the field to hear from people. The problem is that so many people want to be heard from, we inevitably get behind in our schedule.

We discussed this at lunch. I think we are going to establish a SOP where we will never have anymore 1-day hearings. They will always be at least 1½ days, to try to get in as many people as possible.

I have no order of preference. You establish your own order of preference in terms of your testimony. I would re-emphasize that your entire testimony will be submitted to the record. If you so desire, you can merely emphasize the highlights of your testimony.

TESTIMONY OF ROBERT DeBOW, PRESIDENT, COPPER STATE BANK

Mr. DEBOW. Mr. Chairman, Mr. Hatcher, thank you for this opportunity.

I will preface my remarks by stating that I am the president of a 5-year-old community bank located 30 miles outside of Phoenix in a town with a population of approximately 12,000. The town is a bedroom community and has a limited amount of employment. Most of the jobs are service oriented.

My comments will be slanted from the viewpoint of small community banks in Arizona and possibly throughout the country.

The Small Business Administration program, if utilized by the smaller community banks, can be a method of financing a segment of the community that would be unreachable to them because of the lending restrictions set forth by the banking governmental authorities.

For example, a community bank in Arizona with capital of $1 million would be restricted to 15 percent of its capital, or $150,000 loan to any individual or corporation.

We at Copper State Bank found a need in our banking area for higher lending limits than we were authorized. We turned to the Small Business Administration guarantee program to serve this community's needs and, by doing so, were able to reach out and service loans ranging from $300,000 to $500,000. The guarantee program, therefore, filled a very important need in the growth of our community and the growth of our bank.

As time went on, our lending demands began to exceed our deposits and we found it necessary to seek out sources of money. It was quickly determined by management that an ideal opportunity presented itself in that we could sell our portfolio of SBA loans in the secondary market and retrieve a considerable sum of money, thus relieving the pressure on the need for lending funds.

I would like to point out at this time that the average bank in its first few years of development has a capital position of approximately $1 million. So, our capital situation is not unique. It is in line with other community banks throughout the country.

My research indicates that 205 new banks were opened throughout the Nation in 1980 and there were 875 banks opened across the country in the past 5 years. Therefore, the SBA program gives the small community banks a method in which they can reach out and serve a segment of the market beyond their legal lending limitations.

If the 90-percent guarantee was reduced, it would adversely affect the ability of a small bank to participate in the guarantee program by increasing the demand on its limited capital.

The availability of the SBA guarantee program has become an intricate part of the growth of Copper State Bank. Through the program we have placed 14 loans on the books with a total value of $1.5 million. We have several more loans now being processed.

Statistics released by the Small Business Administration indicate that for every $10,000 in SBA lending, one job is created. Therefore, it follows that our bank has been successful in creating a considerable number of new jobs in our community through the program.

As a secondary factor, the bank itself was able to create additional job opportunities and now employs a staff of 47. We continue to utilize the program and soon will be preparing to sell our second package of loans.

Although the numbers and dollars involved in our program would seem small in this day and age when figures in millions and billions are heard daily, I feel it is extremely important to note the success of our community bank's ability in obtaining guaranteed loans for the business community in the area we serve.

In viewing our experience at Copper State Bank in the past 5 years, I must admit that the Small Business Administration programs are not without problems and, at times, seem to be burdened with excessive paperwork.

In my opinion, more emphasis should be given to the bank certified lending program allowing more latitude to the banks in the preparation, credit evaluation, and processing of a SBA guarantee package. This is particularly true in loans of less than $100,000 where it appears, at times, the paperwork required exceeds the value of the loan to the bank.

The privilege of participation in the program should be closely monitored by the Administration, with an eye toward special recognition of the banks with good credit evaluation and performances.

What I am trying to say is if a bank's lending record in the past indicates excessive SBA guarantee loan failure, maybe consideration should be given to restrict them from program participation.

I would further suggest that the $500,000 guarantee program limits be increased to at least $750,000 or $850,000, particularly so when real property is involved in the loan package.

In concluding, I might also suggest to you that losses sustained on bad SBA loans could be reduced considerably if the liquidation of the loan was placed in the hands of the financial institutions that initiated the package.

I realize this suggestion might not be well received by the larger lending institutions. However, as an example, 10 percent of a $400,000 loan, or $40,000, is a large sum to lose for a small community bank, while this size loss could be looked upon routinely by the larger banks.

I believe the initiating institution, in most cases, is more closely related to the borrower, has more flexibility to preserve the remaining assets and can proceed with a quicker, more orderly liquidation, thus reducing the loss to the Small Business Administration and to the financial institution involved.

Thank you very much.

Mr. MITCHELL. Thank you, sir.

TESTIMONY OF JOHN HANSGEN, SENIOR VICE PRESIDENT, BUSINESS LOAN GROUP, THUNDERBIRD BANK, PHOENIX, ARIZ.

Mr. HANSGEN. Mr. Chairman, Congressman Hatcher, my name is John Hansgen. I manage the business loan division of Thunderbird Bank. We are the second smallest bank on the panel. We are pleased to appear before you today in connection with your inquiry into the problems of small business.

With two-thirds of our loan portfolio consisting of loans to small business and 25 percent falling under the SBA guarantee program, Thunderbird Bank is not only committed to, but is dependent upon small business.

We have been particularly aggressive in utilizing the SBA guarantee program, primarily because it answers four of the major problems facing small business today: The inability to raise capital; lack of accessibility to financial markets and the Government programs available to larger companies; the inability to cope with widely fluctuating and abnormally high interest rates; and the inability to internally generate and maintain suitable equity ratios due to the destructive impact of inflation on the balance sheet, and a tax policy which confiscates capital needed for expansion, and in some cases, survival.

Thunderbird Bank has had sufficient longevity in the program to recognize the benefits. We have made 250 SBA loans since 1972, totaling $37 million. We currently have 155 loans outstanding, to some 135 business entities, approximating $22 million. Bear in mind our total loan portfolio is only $82 million.

Let's look at the result. We conducted a survey last month, the month of August, which covered 99 companies. We received responses from 78 of these. The 78 respondents represented $12.6 million in guaranteed loans. This was equal to 64 percent of our total guarantee commitments outstanding.

It is interesting to note these companies employed 2,702 people. They remitted $4,784,000 in withholding taxes on behalf of these employees; 51 of the 78 companies reported paying Federal income taxes totaling $1,107,000. That is more than General Motors, Ford, Chrysler, and the airline industry combined, paid last year, I believe.

Of the 27 companies reporting no Federal income taxes, it should be noted that 17 of these were either individual proprietorships or subchapter S corporations, and taxes were paid by the individual. The balance either had a tax loss carried forward or were unprofitable.

Let's look at losses as reported by the SBA. Chargeoffs against our loan since 1972 totaled $415,000. This was offset by $330,000 in guaranteed fees paid. I wish I could say this is the full extent of the loss. However, the entrepreneurs who took the risk suffered far greater losses through dissipation of personal assets and time and wages lost even though the loans were partially or fully repaid.

I don't believe that either the successful companies or the ones that failed owe anyone an apology. In fact, it is quite obvious that the taxpayer and the community are the primary beneficiaries of the program.

I strongly urge the committee to devote some attention to the preservation and strengthening of this program, which has proven most beneficial to both small businesses and the community.

Some observations are as follows:

Guaranty maximum. The maximum guaranty was $350,000 in 1972 when I began working the program. This obviously has not kept pace with the increased costs associated with starting or operating a business.

I would caution the committee that failure of the maximum to keep pace with escalating costs will eventually result in the program being channeled into the areas of lowest economic return and the greatest competitive risk to the detriment of the people we are trying to help.

Interest rates. The present structure appears to provide adequate flexibility for both lenders and the secondary market. However, proposed changes would result in an increase in interest rates to our customers and could also discourage the participation of both lenders, including ourselves, and the secondary market.

The interest rate structure should continue to provide the flexibility necessary for participation of lenders and still permit competition to function for the benefit of the small business community.

Size standards. I believe the deficiencies in this are are well recognized and are being addressed.

Guaranty percentage. The existing 90-percent maximum should be maintained. Failure to do so will result in a number of companies being unable to obtain financing.

Consistency. Very important. Change proposals, such as the current one on interest, narrow and differing interpretation of the program's intent, and the constant threat of rule changes do little to further utilization of the program.

While a small bank such as Thunderbird can react rapidly to change, it should be recognized that larger organizations must devote considerable planning, effort, and expense in preparation for participation.

Guarantee funds appropriation. There has been considerable recent discussion with regard to reducing appropriations. I understand this is now an accomplished fact. This does not appear to be a proper approach to assisting small business, particularly in view of the economic returns being realized. A reduction hardly seems compatible with supply side economics.

In summary, I would urge the committee to not only focus on the many unanswered problems that do exist with regard to the disadvantaged and small business, but to also be alert to the misguided efforts to curtail or eliminate programs which have proven to be so beneficial.

Thank you.

[Mr. Hansgen's prepared statement with attachments follow:]

PREPARED STATEMENT OF JOHN HANSGEN, CPA, SENIOR VICE PRESIDENT, BUSINESS LOAN DIVISION, THUNDERBIRD BANK, PHOENIX, ARIZ.

Mr. Chairman and members of the committee, I am pleased to appear before you today in connection with your inquiry into the problems of the small business community in Arizona. Thunderbird Bank has had a clearly defined policy level commitment to small business since being chartered some seventeen years ago. This policy determination was due both to the recognition of the market place and the competitive environment.

This philosophical dedication to serving the small business community has proven beneficial to the bank as well as the market segment served. Today, Thunderbird Bank ranks eighth among Arizona banks with $125,000,000 in assets and $82,000,000 in loans. All growth was generated internally, without the benefit of acquisitions, and can be directly attributed to recognizing and targeting on the small business sector which, at the time, was not being adequately served by the larger institutions. I might add that the competitive environment today has changed dramatically. Both the large, local and money center banks now recognize the importance of this market segment and are making a concerted effort to capture their share of the market.

Thunderbird Bank established the Business Loan Division in 1975 for the specific purpose of serving the small and medium size business. I, personally have managed the division since formation and have been directly involved in financing these businesses for the past ten years. Of our $82,000,000 loan portfolio, approximately two-thirds consists of loans to small businesses. The bank is a certified lender under the Small Business Administration BCP program and is considered to be a leader in the State of Arizona in the utilization of the guaranty program.

Our unique experience in serving this particular market segment has made us well aware of the all too familiar problems confronting small business, such as:

1. Inability to raise capital;
2. Lack of accessibility to the financial markets and the government programs available to larger companies;
3. Inability to cope with widely fluctuating and abnormally high interest rates;
4. Inability to internally generate and build suitable equity ratios due to:
   - (*a*) The destructive impact of inflation on the balance sheet;
   - (*b*) A tax policy which confiscates capital sorely needed for expansion, and in some cases, survival;
5. Excessive governmental regulation and reporting.

I'm sure the committee is already cognizant of the above problems. I will therefore direct my observation to one program, already in place, which has been of the greatest benefit to small business—specifically the Small Business Administration Guaranty Loan Program.

It seems the SBA is constantly under attack and I'm sure abuses do exist in some of the programs. However, I would caution the committee to not lose sight of the programs which have proven themselves and are rewarding.

Thunderbird Bank, while one of the smaller banking institutions in the state, is eminently qualified to comment on the program by virtue of having made more loans, currently having more loans outstanding and reportedly having a better success ratio than any other bank in Arizona.

I recognize that mere utilization of a program does not demonstrate its effectiveness. However, let's examine some statistics which we have accumulated since 1972:

[Dollars in thousands]

	Number of loans	Amount
Loans made since Jan. 1, 1972	250	$37,069
Outstanding loans at July 31, 1981	155	$21,889
In process at July 31, 1981	17	$3,875

Note: Losses or chargeoffs against the guaranties from 1972 through September 1980, as reported by the SBA, totaled $414,649. To date, this is a nominal 1 1/10 percent of total guaranties committed.

We just completed a survey of the companies in the portfolio with regard to employment and tax revenues generated. Unfortunately, for various reasons we could not obtain 100 percent response. However, the following does represent 64 percent of the loan amounts outstanding and a 79 percent response of the companies surveyed.

Number of companies surveyed	99
Number of companies responding	78
Amount of SBA loans outstanding	$14,006,000
Amount of SBA guaranties outstanding	$12,606,000
Number of employees	2,702
Federal withholding taxes remitted, latest fiscal year	$4,784,000
Federal income tax paid, latest fiscal year	$1,107,000
Withholding taxes generated as a percent of guaranties outstanding	37.95
Federal income tax generated as a percent of guaranties outstanding	8.78
Total taxes generated as a percent of guaranties outstanding	48.73
Guaranty dollars per employee	$4,665

In reviewing the above statistics, it should be noted that, of the 78 companies reporting, 27 reported no Federal Income Tax Liability for the following reasons:

1. Seventeen were either individual proprietors or sub-chapter S corporations and income would be reported individually.

2. Two were quite profitable but incurred no liability due to tax loss carry forward.

3. Eight were either in the startup phase or had not completed a full year of profitable operations.

It should also be recognized that the above survey did not include a number of concerns benefiting from the program that no longer have any outstanding indebtedness. However, these businesses are continuing to generate employment and tax revenues.

I'm sure the committee will agree that the above certainly substantiates the viability of the SBA guaranty program. Bear in mind, that while a guaranty commitment does exist, no governmental or taxpayer funds are invested in these companies other than program administration costs. In fact, the only other funds invested have been the $415,000 in guaranties charged off and even this amount has been partially offset by approximately $330,000 in guaranty fees paid. The successful companies will continue to generate employment and tax revenues long after their loans are fully paid.

I strongly urge the committee to devote some attention to the preservation and strengthening of this program which has proven most beneficial to the small business community. Some observations that should be considered are as follows:

1. *Guaranty maximum.*—The present guaranty maximum is $500,000 as compared to $350,000 in 1972, when I began utilizing the program. This is an increase of 43 percent in ten years. This obviously has not kept pace with the increased costs associated with starting or operating a business.

Failure of the guaranty maximum to keep pace with escalating costs will eventually result in the program being channeled into the areas of lowest economic return and greatest competitive risk to the detriment of the people we are trying to help.

2. *Interest rates.*—The present structure appears to provide adequate flexibility to the lenders and the secondary market. However, proposed changes would result in an increase in interest costs to our customers and could also discourage the participation of both lenders and the secondary market.

The interest rate structure should continue to provide the flexibility necessary to the participation of lenders and still permit the competitiveness of the market place to function for the benefit of the small business community.

3. *Size standards.*—These are completely obsolete and void of fact, reason and logic. A perfect example is the filling station owner whose sales volume now exceeds the sales dollar size standard, not because of an increase in unit volume, but because of increased costs which were completely out of his control.

Consideration should be given to expanding eligibility, revising the standards and indexing, where required.

4. *Guaranty percentage.*—The existing 90 percent maximum should be maintained. Failure to do so could result in a number of businesses being unable to obtain financing. This includes the high technology area which carries substantial risks but also produces the greatest returns.

5. *Consistency.*—Change proposals (such as the current one on interest), narrow and differing interpretations of the program's intent, and the constant threat of rule changes do little to further utilization of the program.

It must be recognized that, while a small institution such as ours can react rapidly to change, larger organizations are required to devote considerable effort, planning and expense in preparation for participation. On numerous occasions, I have seen larger Phoenix institutions prepare for active participation only to be discouraged by some unwarranted action or proposed change in the rules.

6. *Guaranty funds appropriation.*—There has been considerable recent discussion with regard to reducing guaranty appropriations. This does not appear to be the proper approach to assisting small business, particularly in view of the economic returns being realized. A reduction hardly seems compatible with "Supply Side Economics."

In summary, I would urge the committee to not only focus on the many unanswered problems that do exist for small business and the disadvantaged, but to also be alert to the misguided efforts to curtail or eliminate programs which have proven to be beneficial.

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The 5 Best Managed Companies In Arizona

Good management incorporates a broad range of factors—productivity, effective research and development, depth of expertise, personnel policies. Most of them are difficult, if not impossible to measure. So, in selecting TODAY'S BUSINESS' list of best-managed companies, special importance was given to those factors which can be quantified—namely, profitability and return for investors. Not by coincidence, most of the other characteristics sought in good management are also displayed in the five companies chosen.

To come upon that list, a thorough analysis was made of the financial records of all public companies based in Arizona. Five of them, considered for their sustained performance over the past five years, as well as compared to others in their industries, where appropriate, quickly floated to the top: Inter-tel, W.A. Krueger Co., Thunderbird Bank, Tucson Electric Power Co. and Miller Technology & Communications. Clearly, different industries and the variance in size provide different opportunities for growth. Utilities obviously are regulated by outside forces, as are financial institutions by uncontrollable monetary policy.

By selecting only five well-managed companies, we do not intend to withhold credit where credit is due. Indeed, another six companies out of the more than 45 analyzed demonstrate admirable earnings and deserve an honorable mention: Circle K Corp. (Phoenix), Canyon Savings and Loan (Prescott), United Bancorp of Arizona (Phoenix), AZL Resources (Phoenix), Continental Bank (Phoenix), and Southwest Forest Industries (Phoenix).

Jeffrey P. Wright, a chartered financial analyst, compiled and reviewed corporate records in preparation for this report. He is president of J.P. Wright & Co., a business valuations firm in Scottsdale.

THUNDERBIRD BANK

Market Strategy Puts Little Guy In the Money

Considering the media blitzkrieg its competitors have waged in recent years, one might surmise that quiet little Thunderbird Bank has been having a rough go of it. But there's a good reason for Thunderbird's apparent aphony: it's carved out a robust market in small-business lending that defies a mass-market approach. And as a by-product of that stunningly profitable strategy, chairman and former president Robert W. McGee has avoided some of the snares of modern-day banking in which many competitors have become entrapped.

More than two-thirds of Thunderbird's business, with assets of $112.7 million (Dec. 31, 1980), is in the form of loans to small firms. Policy has lent primarily to individuals and firms who produce, rather than consume, goods and services. Other banks have gone after retail business—personal checking accounts, loans and savings. "But nobody was looking after the grubby little machine shop that needed a fifty- or sixty-thousand-dollar loan," says Victor H. Frank, executive vice president and chief credit officer.

By sticking to commercial lending as its bread and butter, Thunderbird has seen revenues soar from just over $4 million in 1975 to $12.5 million in 1980, and return on the average shareholder's equity more than double in the five years prior to 1980. Many other Arizona banks have shown similarly admirable growth during the last several years, much of it largely tied to the spectacular growth of the state. But Thunderbird has accomplished its earnings with a relatively subtle approach—certainly with less public attention—merely by the nature of the market it's pursued.

Since it's concerned with reaching the corporate account, Thunderbird has skipped expensive mass-media advertising, the cumbersome administration of consumer loans, and avoided the scramble of others into mercurial branch expansion, automatic teller machines and Saturday openings. And by staying away from heavy consumer business, the wave of expensive and complicated consumer lending laws passed in the 1970s, such as Truth in Lending, have affected Thunderbird only minimally.

But the beauty of Thunderbird's strategy, and the reason for their superior performance, has been much more than a de-emphasis of retail banking. It's been a very aggressive pursuit of commercial lending at the grass-roots level, with the largest portfolio of Small Business Administration-guaranteed loans of any bank in the state as its centerpiece. With government guarantees, SBA loans are very marketable to secondary buyers. So its large SBA portfolio has bolstered Thunderbird's liquidity as well as its profit margin, since SBA interest is tied to a variable peg rate that fluctuates less radically than the prime. The result has been stability of earnings and happy customers who have kept afloat despite the unweildy rise of interest rates for traditional sources of funds.

"We're a net generator of funds," boasts chairman McGee. "The last time we borrowed consistently was 1974-75."

While other banks tend to funnel commercial lending to a few branches and/or the home office, each of Thunderbird's branches is responsible for generating and servicing its own accounts. That autonomy in the field, despite its relatively few branches, McGee says, has kept Thunderbird competitive and, indeed, the dominant commercial lender to small businesses in the Valley. Thunderbird has achieved that distinction largely by emphasizing personal service by maintaining the same personnel at the same branches over many years, thereby providing consistent and personal service to its customers. Once a branch loan officer establishes business contacts, his salary is likely to be raised to the level he would receive were he to move on to a higher position at a different branch—just to maintain that all-important consistent and personal contact. "The customer does his business with our branches, not the corporate office, so that the competition for commercial accounts becomes the next closest Valley National or First National branch," McGee says. "And if their expertise and personal knowledge of the customer's business isn't as great as ours, we'll get the business."

Thunderbird's 10 branches are backed up by a four-man business-loan team from the corporate office that offers technical expertise in support of branch managers. McGee calls them his Green Berets—his front-line marketing artillery—and gives them free reign, free cars and country-club memberships with which to stay at the center of business circles.

Management's support of its personnel at Thunderbird does not stop at the front line, rather it filters to the lowest of the ranks. In the bank's first promotional effort in years, the "100/100 Program" in 1981, the staff of 160 set a goal to push assets over the $100 million mark during the 100-day period prior to May 3, the bank's fifteenth anniversary. When the goal was reached four weeks ahead of schedule, management awarded everyone, from the executive vice president down to the janitor, a $100 bill. "McGee's a tremendous administrator," says one branch manager. "He makes every employee feel a part of it."

While competitors, clamoring in an increasingly competitive retail marketplace, have begun to see the light Thunderbird has been emanating for years, McGee and credit officer Frank are confident their foothold in commercial lending will stand them in good stead. Given their past success, it's appropriate that Thunderbird's new president, James S. Lee, has considerable commercial lending experience from the past 19 years with Arizona Bank. "A good commercial lending officer should be running this bank," McGee says. "That's how we started."

—By Jon Levine

Thunderbird Bank - Buyers list at home office

Recent Price: $75.00	Dividend: 2.00	Yield: 2.67%	
	1978	1979	1980
Revenues (000)	5,746	8,489	12,504
Earnings per share	8.15	9.44	16.12
Return on equity	21.02%	20.26%	27.96%

Mr. **Mitchell**. Thank you.

Mr. Perin, please.

TESTIMONY OF E. DANSON PERIN, EXECUTIVE VICE PRESIDENT, ARIZONA BANK

Mr. **Perin**. Mr. Chairman, I am Dan Perin. I am in charge of commercial and consumer lending activity at the Arizona Bank.

I appreciate the opportunity to appear before you. I would like to read part of my testimony.

Mr. **Mitchell**. No problem.

Mr. **Perin**. One of the most obvious and visible problems confronting all businesses, large and small, is the current level of interest rates. The high rates that we are presently experiencing and which have been with us for an extended period of time are particularly burdensome to small business.

Small businesses do not have access to national or international financial markets, nor can they take advantage of some of the more exotic forms of financing available to larger companies. I might also add that this holds true for many of the smaller, local and regional banks who provide financing to the small business community.

As borrowing costs cut into profits, small business finds it increasingly difficult to generate sufficient capital in the form of retained earnings to sustain their operations and provide for growth, and in today's environment, raising new outside equity capital becomes virtually impossible.

The present rate structure has also dramatically changed the way people do business and the environment in which a small business has to operate. Individuals and the larger companies have become very adept at cash management which refers to a whole variety of techniques used by businesses to speed up the collection of receivables on the one hand and to take maximum advantage of trade terms on the other.

A lot of these cash management tools are simply not available or applicable to small businesses, at least to the extent that they might be in larger businesses, and to the degree that a small business is dealing with companies that do utilize these techniques, it results in additional borrowing requirements and higher interest costs.

Today's rates also inject more risk into the economy, and the small businessman or woman must be increasingly careful about whom they do business with.

Today's high rates have a particularly severe impact on the Arizona economy. For better or for worse, we do not possess a large diversified industrial base. The energy activity that has produced phenomenal growth in places like Houston, Dallas, and Denver simply isn't there.

Recently, we have experienced an inflow of electronics and high technology-related companies, and those businesses have provided important support for our economy. Basically, ours is a service economy and our growth has come from many sources.

People perceive Phoenix as an attractive place to live and raise a family. Tourism and the resort business has also been important to our economy and, of course, many people have chosen Arizona as a place to retire. As a consequence, the residential construction industry is an extremely vital element of our economy, more so than it might be in other cities.

Today's high rates have severely depressed the housing market and residential construction activity, and many of the small businesses which directly or indirectly service the construction industry are experiencing difficulties.

As I have moved around the State, I have become increasingly impressed with the degree to which our economy is dependent upon the residential construction business. We don't have an economy like Denver, Houston, or Dallas that is fueled by, in their case, the energy program. As a consequence, the fortunes of small businesses in this community in many cases are very, very closely tied to the fortunes of the construction industry.

In this particular city, that industry is suffering severe problems. I understand new housing starts in the third quarter of this year projected by one official that we consult with to be the lowest in 10 years. That is a severe problem.

I notice there are a lot of contractors in the room today. So that is a particular problem for this economy. More so than perhaps other cities.

Another problem which faces the small and disadvantaged business community has to do with communication and knowledge or lack thereof regarding the many counseling and other professional services that are available.

I think the problem is particularly acute in the lending area. Applying for a loan can be a very intimidating experience for many people, and at best is probably confusing for those who have not established close banking relationships.

Many small businessmen simply don't know where to apply for a loan, what services are available, what terms best suit their particular needs, and what information the bank needs or the criteria it uses to evaluate a request for credit.

I am sure that many small businesses which could qualify for and take advantage of various private and Government-backed loan programs do not because of the perceived difficulty in getting a loan or because they simply don't know where to start.

These are just some of the problems that face the small business community today.

With regard to rates, the banking industry can and has taken some steps to provide relief for small businesses. Many banks have the capability to provide level payment programs despite the fact that the rate charged the customer floats with prime.

These kinds of programs in effect defer interest charges into the future, and while they do not reduce the overall financing costs for a business, they do allow a business to better manage its future cash flows. Also, in certain circumstances, banks have accepted lower margins over their cost of funds as rates have climbed to higher levels.

While we do not like to steer good business away from the bank, we have often directed our customers to other lenders if we felt there was a significant advantage to our customer for doing so.

Many banks in this community have been active participants in various SBA loans. These programs represent a vital source of capital to small businesses and its services are needed more than ever.

The SBA, in connection with private groups, also plays an important educational role through its various counseling programs. Despite the best efforts of everybody involved, these programs probably reach a small handful of those who could or should avail themselves of these services.

I would encourage more active participation between the SBA and the banking community in providing needed counseling services, and I think you would find most bankers quite receptive to that suggestion.

Let me very quickly address a few of the proposed changes to SBA business loan policy. Specifically, I would like to comment on those rules regarding the maximum guarantee loan, the percentage of loan guaranteed, the maximum allowable rate, and the handling of the guarantee fee, as well as the suggestion that the banks be responsible for collection of delinquent and past due loans.

With regard to the maximum guaranteed loan, we support the SBA request to raise the limit from $500,000 to $750,000. We simply feel that the higher amount more properly reflects the financing and capital needs of the small business community and gives proper recognition to the effect that inflation has had on individual borrower financing requirements.

With regard to the proposal to reduce the percent of guarantee on loans over $100,000, we feel this is a reasonable and acceptable solution to the budgetary constraints facing SBA, and we don't feel this would have a negative impact on the program.

The suggestion that the banking community take more responsibility for collecting past due and delinquent loans has some merit, but also presents some problems.

To the extent that such an arrangement results in faster and better collection experience, it would prove advantageous to both the banks and the SBA. On the other hand, the lending institutions would have to incur additional costs; not just direct recovery costs, but the salary and benefit costs associated with additional staffing.

We feel the guarantee fee should be passed on to the borrower, and we do not agree with the provision in the House bill. The conference substitute regarding notification is acceptable and conforms to existing practice.

Finally, I would like to discuss the proposed change regarding SBA interest rates, specifically that the maximum acceptable interest rate would be limited to the minimum money center or New York prime rate printed in the Wall Street Journal.

We have great difficulty with this proposal. Money center banks are very different animals than regional or local banks. Their asset mix is different and, more importantly, the major New York banks fund themselves worldwide on a 24-hour basis.

They have many more sources and far more flexibility to finance their lending activities than are available to most banks, and certainly most regional and local banks. The prime rate of a particular New York bank on any particular day reflects its marketing strategy and its funding costs, which have no relationship to the way we operate our business here.

If we followed the proposed rules limiting the maximum rate to the lowest New York prime, in effect we would be providing preferred rates to our SBA borrowers relative to our other good customers, and I don't think that is proper, nor do I feel it is the intent of this legislation.

I think it is important to consider the impact of these various changes not only individually on their own merits, but together as a package. While no one item would severely diminish the attractiveness of this kind of lending, with the possible exception of the interest ceiling, all the proposals, if enacted, would mean that the banks which continue to participate in SBA lending programs would be faced with higher risks, higher costs, and lower margins.

Banks throughout the country are suffering from substantially higher costs due to deregulation, and every bank in the country is becoming increasingly concerned about yields and allocation of assets.

I think in constructing this legislation we have to be very careful to avoid changes, such as the interest rate ceiling, which would have the perverse effect of discouraging participation by lending institutions in the SBA programs which are so desperately needed by the small business community.

Thank you.

Mr. **Mitchell**. Thank you very much.

TESTIMONY OF NATE COLLINS, VICE PRESIDENT OF CORPORATE BANKING, VALLEY NATIONAL BANK

Mr. **Collins**. Mr. Chairman, Mr. Hatcher, I am Nate Collins, with Valley National Bank. I am pleased to appear before you today in connection with this inquiry into the problems of the small business community in Arizona.

I would like to begin by giving you a brief background into the small business climate in Arizona today. Our current statistics show there are 42,595 businesses in the State. Of that number, 37,003 are identified as small businesses. They constitute almost 98 percent of the total marketplace.

Let me point up at the outset that our bank identifies small businesses as those companies with $5 million or less in annual sales, however, our participation with the SBA obviously is based on the various size standards at the Agency and is not limited to our general marketplace evaluation of $5 million.

The top three industries—retail trade, services, construction—account for 72 percent of all businesses in the State including small businesses. Records indicate that these three industries share a nearly equal proportion of the total marketplace in Arizona. For example, retail trade accounts for 30 percent of all Arizona businesses, services is 26 percent, and construction is 16 percent.

In the 4 years since 1977, the total economic business growth has been 18 percent statewide. During this time, small business almost matched that figure with an increase of 17 percent in the State and an 18-percent increase in Maricopa County.

Therefore, we think we can say that Arizona represents a supportive market where small businesses can flourish. We believe this is substantiated by a recent report from Dun & Bradstreet showing that Phoenix experienced a 54-percent decrease in failure for all businesses from 1979 to 1980.

I was really trying to profile a little bit of what we see at our bank as the small business environment in this State. We have trouble dealing with the size standards that SBA uses, so we simply look at a $5 million annual sales below which we consider to be small business.

Be that the case, 98 percent of the business in this State is small business. I think history has proven that small business has prospered pretty well in this State. Therefore, this panel and the panels you have had through the day are speaking for a pretty good profile of small business in the Southwest.

The three major areas of small business—retail trade, services, and construction—are easy to start because of low capital investment and subsequently have an opportunity to grow rapidly in our normally flourishing economy.

But therein lies a problem. Their small capital beginnings may become more strained as their sales growth increases because they may not be able to retain enough of their profits in the business to support the growing needs for receivables, inventory, plant, and equipment. This tends to create growth-dependent, highly leveraged companies.

In the current environment, the small business person is experiencing a slowdown in sales activities, heavy debt servicing requirements, and unprecedented high interest rates.

Any one of these elements can be found across the country, but I suspect that in Arizona it is more intensified because all three of these elements prevail, particularly heavy debt service.

Therefore, we can see that this current situation is fraught with problems that may not be of the making of the small business person, but more frequently due to the economic environment they find themselves in today.

We know from national statistics that 9 out of every 10 business failures can be traced to managerial deficiencies. It would appear, therefore, that there are numerous small business owners out there who have limited, overall business skills.

We have talked at length to many of our branch managers and loan officers, and this is what they have told us about the problems of the small business person.

One, many of them don't know how to approach a financial institution for any banking services, but particularly for credit.

Two, they don't know about establishing workable loan structures, such as short- versus long-term financing plans.

Three, they rarely come into the bank with adequate legal and/or financial counseling.

Typically we have recognized that the small businessperson is the one who has a certain expertise in the development of a product or service, but he or she has little or no experience in the managerial, legal, personnel, accounting, or financial aspects, all of which are essential to a successful business. They also must cope with growing Government regulations that even further hinder their ability to succeed.

Another problem we encountered was with our own loan officers, at least in our bank. I better not talk to the others.

The often find that they do not have a thorough understanding of SBA programs. When a person comes to the bank for advice, a loan officer frequently discovers that he or she does not have the necessary background to answer a lot of those questions.

We would suggest that the SBA consider expanding its educational efforts with bankers so they would feel better equipped to handle such matters.

As the largest bank in Arizona, with offices in nearly every community in the State, we feel a major responsibility to every phase of the business community.

We try to staff a branch in each economic center with loan officers that can deal with any appropriate commercial loan request presented to us. When we receive such a request, we consider it to be our responsibility to evaluate its substance and recommend alternatives, when appropriate, in a timely manner.

Among those alternatives that we may suggest would be the type of credit arrangements that may only be bankable with a secondary or external support source, such as SBA guarantee. This usually is considered when the business concept is felt to have a successful potential but may require longer credit terms; that is, lower payments than would be normal bank practice. Working through SBA will allow us to offer proper financing to the applicant.

In consideration of this, we recognize a responsibility both to the potential borrower and to the taxpayer. In terms of the borrower, our responsibility is to assist that person with his or her endeavors in starting a small business, if appropriate, or conversely to deter them from their efforts if we feel that the borrower faces a high probability of failure.

As for our responsibility to the taxpayer, we obviously will not recommend loans that have a high probability of failure, creating sizable losses to SBA.

Our own bank programs also address the problems of the small business customer.

We have conducted financial education seminars which have been largely attended by small business owners during the last several years. Emphasis has been on specialized services, such as trust information and computer systems.

I have some discussion on the minority situation in Arizona. But frankly, as you have heard I think from other testimony, and we would support, there is very little data we could speak to that would have any substance to what we might present.

I do discuss a little bit of women in business, which would probably be germane to the previous testimony. There has been some effort with all the banks in the State to put on seminars, if you will, in training women in business by women loan officers. That was a rather successful seminar we held about 6 months or 1 year ago.

There are approximately 5,200 women business owners in Phoenix compared to 20,000 in Chicago. Research indicates that many women have been discouraged from expanding their enterprises because of inexperience in working with banks and companies which provide venture capital and loans.

In realizing this, the National Association of Bank Women conducted two pilot projects, one which was held last March in Phoenix. Eighteen women business owners attended. Forty-six bankers, half from Valley National Bank, conducted the sessions. Emphasis was focused on identifying financing sources, assessing financial business needs, preparing a loan request and negotiating the loan. The women told us they wished they had had this knowledge when they went into business. They felt this information would have saved them time and money and prevented stressful situations.

In addition to that, however, there is another area that some of the banks in the State are working on, and that is working with a nonprofit organization known as the Chicanos Por La Causa.

Two other banks have been working with us investigating a program to develop an independent corporation for that organization whereby they could make loans to small businesses that the banks would not normally consider. Each bank would contribute a share of the capital for this program. This is simply a local community effort on the part of the banking industry.

We are well aware of the dependence of all businesses in an economic environment upon each other, be they large or small. The small companies as suppliers and/or customers to the major corporations cannot be stifled with nonproductive regulations. Likewise, the major corporations must be relieved of onerous regulations in order to preserve a healthy business community.

Many firms have expressed to us their concern over how long they can continue to be supportive of one another under excessive regulations. I think you have all heard a lot about that. Rather than dwell on it too long, I want to discuss the SBA as we perceive it.

However, there is one regulation that you might find of interest, and that is the problem that ERISA has given the small business community.

When the Employment Retirement Income Security Act became law, its impact caused thousands of small employers to terminate the employee benefit plans. The primary reasons were the extensive reporting and recordkeeping requirements needed.

When this act was established, the Internal Revenue Service promptly issued 250 pages of regulations governing the Nation's private pension programs.

Within months, 13,000 of these plans were terminated. Many of the firms, with less than 30 employees, simply could not meet the immense cost increases entailed in the regulations.

By losing this employee benefit availability, those small businesses lost one of their primary tools in which they could compete in the employment marketplace. We think they are being penalized simply because they are small. Now back to SBA.

We view the main areas of SBA support for small businesses to be financial assistance, management assistance, procurement, and assistance to disadvantaged entrepreneurs.

We believe that SBA has the tools both legislatively and administratively to deliver quality services in the area of management assistance, procurement, and assistance to disadvantaged entrepreneurs.

However, in our opinion, the SBA could do a better job of communicating this ability to the business community and it, in turn, could do a better job of executing its functions. But the framework of legislation is there to provide it, if done well.

In the area of financial assistance to small business, SBA can look at several ways of improving their programs. For instance, it might be helpful to pursue some type of interest rate relief through tax programs.

Second, tax deferments for property transfer within family-owned businesses should be considered. More often than not the small business is a family business that has been passed down from generation to generation.

Some tax deferral program permitting that same generation-to-generation passage would help foster the continuance of successful small businesses. Every dollar that is taxed out of that business serves to erode the future continued success of it.

Third, higher dollar amounts for guarantee loans could be made available. The maximum loan has been $500,000 for several years. Inflation would suggest this figure should be higher and still it would be used as a financial support for businesses that are truly small.

Finally, the SBA might consider establishing loans with variable maturities. Such loans would allow the lender to have a variable rate of interest, but the bank could set up the loan payments at a constant level. Thus, higher interest rates would create a loan with a longer life, while lower rates would create a loan with a shorter life.

SBA has been proposing a maximum interest charge at prime rate. If this were to happen, we think many financial institutions would be taken out of the market because the cost to administer these smaller loans is much higher than the regular commercial loans.

For this reason alone, the higher rate is justified. Further, our experience has been that wherever consumer interest rate limits occur in times of high rates, credit availability ceases rather than limits the cost to the borrower.

If the SBA guarantee percentage is lowered, you will find that this will not increase the number of loans but will dramatically decrease them because of the higher loss exposure to the lender.

What would it mean if the qualifying standards for SBA loans were increased? In our case, higher standards would surely mean far fewer SBA loans.

In the regulatory environment we find ourselves in today, free enterprise is being threatened and may only survive in those businesses large enough to cope with it.

Because of regulations, small businesses are not in a free, competitive environment. They should be viewed in a somewhat different light from those large businesses that can cope better with the regulatory burdens of today.

Finally, let me reemphasize our bank's continued support for the programs offered by the SBA and our continual commitment to the small business community in Arizona.

The small business economy has been deeply imbedded in the heritage of this country for centuries. It is one of our most vital resources today. Like many other Americans, small business owners are deeply disturbed about inflation and regulatory burdens. These entrepreneurs represent a vocal and forceful strength for the eighties that none of us can ignore.

Thank you.

Mr. MITCHELL. Gentlemen, I thank all four of you for very, very interesting testimony. Let's see what we can sort out.

First of all, there appears to be an absolute consensus that the maximum guarantee loan limit should be increased. Is that correct? We are talking somewhere in the area of $750,000 to $850,000.

Now, I sense, however, that there is not a consensus with reference to reducing the percent of the guarantee on loans. It is now a fait accompli, unfortunately. I hope the Congress will be able to turn that around next year or the following year.

As you know, any loan in excess of $100,000 you have at the discretion really of the SBA Administrator to range between 70- and 90-percent guarantee. Now, I believe it was your testimony that said that you found that fair and equitable. Yet, I got the impression from the other three witnesses that would be detrimental. Am I correct?

Mr. PERIN. Yes.

Mr. HANSGEN. Mr. Chairman, I think the 90-percent guarantee need be maintained, particularly on those loans of $100,000 or less. But our experience has been that the larger the loan, the lower the risk.

I see nothing wrong with lowering the guarantee progressively as the loan increases in size.

Mr. MITCHELL. Then you see nothing wrong with the present formula?

Mr. HANSGEN. Right.

Mr. COLLINS. I would disagree with that. It depends on how your bank, Congressman, uses the guarantee. I think that we could portray our use of the SBA guarantee as kind of the lender of last resort, if you will.

In our portfolio, it is the highest type of risk that we would be looking for the guarantee. If that guarantee is reduced from the 90 on down to a 70 kind of level, that presents us with an exposure at which point we would probably back away. We might send them over to John.

Mr. DEBOW. Mr. Chairman, I come from a little different approach. As I stated in my testimony, I am concerned about capital and how much money we are allowed to invest. Therefore, a reduction would lean heavily on the amount of funds that we have available and reduce the number of loans that we could place.

Mr. MITCHELL. All right.

I recognize the minority population in the State is relatively small, counting blacks, Mexican Americans, and so forth. But as I review the data that is before me, I get a little concerned.

From 1979 to 1981 the SBA approved 46 loans for $6.5 million in the Arizona Bank. Of these, one loan of $42,000 plus was to a woman and one loan of $47,000 plus was to a minority.

On the Thunderbird Bank for that same period the SBA approved 109 loans for $16.8 million through this bank. Nine loans of $1.2 million went to women, and 28 loans of $109 million went to minorities, for the amount of $4.8 million, which is not bad.

The Valley National Bank in the same period, SBA approved 95 loans for $10.9 million. Of these, 13 loans went to women, $1.2 million, and 13 loans went to minorities, $1.6 million.

Is the problem that the SBA is not referring minority packages to you? Or, is it that there is a prior turndown?

Mr. PERIN. In our case it is a function of a couple of things.

Mr. MITCHELL. I am sorry. I really didn't get my question out. Is it that they are not referring, or is it there is a higher turndown rate for minority packages written? That is what I want to find out.

Mr. PERIN. I am not sure it is the SBA's responsibility to refer loans to us. I think it is our responsibility to go out and find those opportunities ourselves.

Mr. MITCHELL. The SBA approves them?

Mr. PERIN. Yes. In our case—we had the lowest percentage as a function of several things. We haven't had a branch in South Phoenix. We will have one before the yearend. That has been a real problem in terms of developing business there.

We haven't had a bilingual SBA officer, which I think is absolutely essential if a bank is to develop a good portfolio in parts of this city and in Tucson.

Finally, we have tended to not keep our SBA officers in that job for an extended period of time. We have tended to perhaps promote people too quickly through the organization.

If a person is going to be effective in any kind of business community, he has to be there, to get to know the people, speak their language. That has been a problem for us. All those things are changing, but I think it is largely behind.

Mr. MITCHELL. Any other statements on this problem?

Mr. COLLINS. That is a tough one to speak to, Congressman. In the case of our bank——

Mr. MITCHELL. May I interrupt you just a minute. It sort of refers to the testimony that we received from Dr. Little, where she pointed out that they felt there was undue scrutiny and so forth for women making loan applications.

Since being here, talking to black, Hispanic, and Mexican American businessmen all day yesterday and today, they seem to have the same feeling. That is why I wanted to probe into this area.

Mr. COLLINS. We don't keep a statistical summary, if you will, or data, on our borrowers by origin, ethnic, and the like. So, it would be hard to profile. You gave figures on our bank, I think; 13 women owned businesses and 13 minorities out of a total of how many was that—99?

Mr. MITCHELL. Ninety-five.

Mr. COLLINS. On my testimony we indicated that the total minority population I think was 28 percent, but that would not include women. So we are about half of parity on that, I would gather, if you were to look on that as parity. But we don't really measure or keep statistics on what sort of minority loans we have made, or how many we have that do not have the SBA guarantee.

Mr. MITCHELL. Would it be helpful to do that, though?

Mr. COLLINS. You are probably going to be requiring that of us in time to come, I would expect.

Mr. MITCHELL. Yes; I honestly think that it should be required. I think you would want to do it on your own, primarily because there is this enormous stake in America right now, the investment in minority business enterprise.

I think for your own public relations posture, you should always be in a position of saying, "That is not quite accurate. This is the real picture of what we have done, where we are going with reference to minority business."

Mr. HANSGEN. Congressman, I think there are other regulations that prevent us from keeping those records, too. In our bank we keep none. In fact, the figures you read are news to me. It is a fairly high percentage.

Mr. MITCHELL. Yes; you look pretty good.

Mr. HANSGEN. If you had asked me, I could not have told you. From an approval standpoint, I don't see much difference. From a loss standpoint, I don't see much difference.

I think the key is whether the business has a chance for success or not because the individuals are still risking their time and their personal assets.

Mr. MITCHELL. I appreciate your comments, but you have to weigh those against the perceptions that are extant in the community, as indicated in Dr. Little's testimony and in the conversations I have had with minority businesspersons.

Mr. PERIN. With regard to Dr. Little's testimony, I set an established loan policy in the bank, and I can assure you there is no policy which encourages loan officers to delay loan applications from women or to scrutinize those in any different way than a normal application.

However, having just come here from New York, where my wife was in business—and she is trying to get in business now—there is a very different mentality toward women I think in this State. It is not a matter of policy, but I am sure that there are a lot of men not used to seeing women in business. I think that will change in time.

Mr. MITCHELL. Congressman Hatcher?

Mr. HATCHER. No questions.

Mr. MITCHELL. All right, gentlemen.

Mr. PERIN. Aren't you going to ask about rates?

Mr. CENTNER. Since you raised the matter, what interest ceiling would you suggest on the SBA loan. There are a number of people on what Mr. Mitchell likes to call the Republican side of the aisle who would agree with the chairman about the 90-percent guarantee.

If we were in fact able to put it back to that level for all loans, what interest ceiling would you suggest?

Mr. PERIN. I would not suggest a lowering of the present interest ceilings, which I think are 2¼ or 2½ over prime.

Mr. CENTNER. Part of the concern is that you characterized it as subsidizing small business relative to other good customers. I wonder how many other good customers can come to you with a 90-percent guarantee and give you such a shot at the secondary market.

Mr. PERIN. I am glad you asked that question before lunch. I went back and confirmed what I thought. I think our figures are probably fairly representative of the group.

If you look at our commercial portfolio, we measure our losses as a percentage of our outstanding commercial loans. The Arizona Bank's losses over the years have ranged on the commercial loan portfolio anywhere from 10 to 20 basis points.

Last year, in 1980, SBA's losses as a percentage of gross SBA loans, including the guarantee portion, were 21 basis points. This year, looking at the claims we have submitted and will submit, today it looks like those losses are going to approach 1 percent of our SBA outstanding, which is extremely high.

Despite the guarantee, our losses are as high or in some cases higher than in our regular commercial loan portfolio.

Mr. CENTNER. The suggestions Mr. DeBow had, would they help you at all in recovering your losses there?

Mr. PERIN. Yes, the suggestion that we make more of an effort in collecting loans. I really do think it has merit.

Mr. CENTNER. The reason I ask that, there is a real concern about the interest rates. I guess the real problem is that the small businessman or woman, minority or otherwise, who in a sense is being penalized for the bad accounts, is not only different in many of the ways each of you outline in your testimony, they are extremely different in the way they approach interest rates, too. They don't have anywhere near the capability to generate internal cash flow or other means of financing. In fact, 98 percent of all capital, venture capital acquired by small businesses, is debt financing. They don't as a rule go public. They don't have a rich uncle to borrow from, although that happens, I am sure.

But for the small business—and I would think particularly for the small minority business, which does not usually have a long history or relatives who have had furniture stores and that sort of thing—the capital formation is necessary for the company to start up. Wouldn't you agree?

If the interest rates are prohibitive, they might as well not bother.

Mr. PERIN. I mentioned a loan program in our bank. The concept is you set a quarterly or monthly payment and that payment remains the same, despite the fact that the prime rate may fluctuate. As rates go up, more and more of the payment is dedicated to interest, less to principal.

But the payment does not change. Basically what you do is stretch your payment out, and then there is a balloon payment. A lot of small businessmen that we loan to like that kind of arrangement. It works to their advantage, to our advantage, but unfortunately the SBA payment terms do not provide for balloon payments.

Mr. CENTNER. Well, do you not in fact get minority and small business firms who, on the face of it, would perhaps deserve something less than the 2¾ percent over prime rate that you can charge, but you are penalizing them—certainly not subsidizing them relative to other customers—because of the losses you might have in your portfolio?

Mr. PERIN. I would not charge, with those kinds of losses, an SBA customer different than another customer.

Mr. HANSGEN. I would like to address myself to that question. We price the majority of our SBA loans on the peg rate. Our customers have quite an advantage. That would be eliminated under this proposed interest rate change.

I might also point out, we probably have as much experience as any other bank in SBA loans. It takes a lot more effort working with these loans. Practically all of them run into trouble the first year or two.

I like the idea of a fixed payment schedule.

Mr. CENTNER. If the maximum loan went up to, say, $1 million, first of all it would be easier to package loans for the secondary market, I would think. Would that kind of thing make it possible to be a little more flexible in the rates, since the larger the loan——

Mr. HANSGEN. I don't think you should address yourself to the rate. We all price differently anyway. I think the chief thing you should do is leave the rate in the place where it will attract the lenders.

What you need is more participation in the program to make it available to more people. I think the marketplace, the competitive factor will take care of the rate. If you try to stipulate your rate, you are merely going to drive participants out of the market, which means the loans will not be available.

Mr. CENTNER. When you say marketplace, you are speaking my language. I wonder really if a minority small businessman—if they shopped around with your banks, would the marketplace get them a lower rate?

Mr. HANSGEN. All of our loans are the same rate. We price different from Valley. The chief thing is, if you fool around with the interest rates, you are going to drive them out of the market and drive us out, too, because nobody will be making loans.

The chief thing is to have it flexible enough that the lenders will participate.

Mr. PERIN. One more thing. The paid rate is a better deal when rates are moving up. When rates are moving down, the prime rate moves more quickly than the paid rate, and it is a better deal for the person buying.

I sincerely hope the rates are coming down. I would also hope that people using the prime rate are going to benefit from it.

Mr. MITCHELL. Optimist.

Thank you very much.

We have two more witnesses. It has been a long day. Could we take a 10-minute break.

[Brief recess.]

Mr. MITCHELL. Our hearing is now ready to resume.

We have testimony from Mr. Marvin E. Perry, president of the Arizona Center for Corporate Responsibility. He asked that his testimony be submitted for the record. Without objection.

[Mr. Perry's prepared statement and attachments follow:]

PREPARED STATEMENT OF MARVIN E. PERRY, PRESIDENT, ARIZONA CENTER FOR CORPORATE RESPONSIBILITY

"Bankers standard line is that their first obligation is to protect their depositors. The key word is 'first' and we should note that the Federal government, by extending deposit insurance to virtually every financial institution, has largely guaranteed that protection. Now it is time to turn to a second and third obligation: The service of individual depositors and of their communities."—Dr. Carol S. Greenwald, President, National Consumer Cooperative Bank.

The Arizona Center for corporate Responsibility is a non-profit organization formed to monitor the behavior of corporation and banks located in Arizona in the areas of corporate responsibility, i.e., equal employment opportunity, equal opportunity lending, loans to South Africa and pollution.

Since early 1980, ACCR has been concentrating on getting the Arizona Bank to institute a meaningful and non-discriminating program toward black and other minority businesses. With total assets of $2.2 billion and 92 branches, the Arizona Bank is the third largest commercial bank in Arizona and one of the largest state chartered banks in the Southwest.

In March 1980, ACCR requested information on the bank's loans to South Africa. Mr. Don B. Tostenrud, Chairman of the Board, continued to deny any knowledge of such loans until confronted with undeniable evidence from the New York based campaign to oppose loans to South Africa and from the U.S. Export-Import bank. That material showed that the Arizona Bank was willing to lend approximately $5 million to South Africa's major utility, ESCOM at the height of the Soweto Riots in June 1976 while major money center banks were nervously cancelling commitments to South Africa.

ACCR was very disturbed to further learn from the SBA and the Farmers Home Administration that the Arizona Bank had only extended one loan to a black person for only $35,000 through the SBA and the Farmers Home Loan Administration from January 1, 1976 through May 31, 1980. Although we were unsuccessful in getting the bank to disclose its non-government guaranteed loans to blacks, we have reasons to believe the bank made few if any non-government guaranteed loans to blacks. This is particularly true in that the bank continuously emphasizes that it is very conservative in its lending policy. This position was recently articulated by Mr. Don B. Tostenrud in his May 1981 presentation before the New York Society of Financial Analysts.

After many unsuccessful efforts to seek redress from the bank's management and Board of Directors, ACCR filed a complaint under the Community Reinvestment Act of 1977 with Federal Deposit Insurance Corporation in August 1980. In seeking a broad based support for our position we were fortunate to get a letter of endorsement from Darwin Aycock, Secretary-Treasurer for the Arizona State AFL-CIO among many other community leaders. We were appalled to learn that an official of the FDIC in San Francisco called Mr. Aycock and requested that he drop his support. We felt this was highly improper for a public official to take such a stance. We were informed that Mr. Aycock did later withdraw his support after the bank used smear tactics against me, a former employee of the bank.

It is my opinion that because of my efforts in fighting for equal lending opportunities and equal employment opportunities the bank took very harsh collection tactics against me over a $675.00 Visa card balance which I had agreed to pay.

In September 1980, a Community Organization, Arizona Association of Community Organizations for Reform Now (ACORN), filed a protest with FDIC in San Francisco over housing discrimination by the bank in low income and minority areas and for not having a branch in that area, South Phoenix. After discussions with ACORN over a 3 month period the bank agreed to put a branch in South Phoenix and provide loan counseling to the residents in that area; in exchange ACORN agreed to drop its complaint. ACCR's analysis of the banks proposal for a branch in South Phoenix raises serious questions.

Because of the hostile feeling toward ACCR the bank refused to address the minority lending aspects of our complaint. ACCR encountered equally hostile treatment by Mr. Charles E. Doster, Regional Director of FDIC, and Mr. Ford R. Paulson, Regional Counsel. We expressed our concern to Mr. Roger Hood, assistant General Counsel, FDIC who responded conscientiously to our concerns.

Despite our best efforts, the FDIC Regional Office refused to hold a public hearing in Phoenix, instead insisted upon holding them in San Francisco. Because it would have been overly burdensome for us to go to San Francisco, we were unable to participate in a hearing and the bank's branches were approved.

ACCR thoroughly agrees with Ralph Nader's statement "no regulators have been as prone to prostrate themselves before the vested interests of the regulatees as have banking regulators."

ACCR recommends that the Federal Government enact the following laws:

1. Every financial institution be required to file a detailed financial plan for lending to minority businesses along with goals before obtaining direct or indirect Federal deposits.
2. Every financial institution should be required to publish annually the number and the amount it loaned to various minority businesses.
3. The Federal Government should require that every financial institution present a detailed plan along with goals concerning the use of black and other minority contractors and sub-contractors in the construction of branches, facilities, etc., before their applications are approved for such operations.
4. Before receiving approval for applications, every financial institution over $100 million in assets should state the number of minorities on its board. If there are no minorities, it should state its policy on recruiting minorities for its board.
5. Congress should frequently monitor the responsiveness of the banking regulators to the general public and monitor their fraternization with the regulatees.

SMALL BUSINESS ADMINISTRATION,
Phoenix, Ariz., July 10, 1980.

Mr. MARVIN E. PERRY,
Vice President, The Arizona Center for Corporate Responsibility,
Phoenix, Ariz.

DEAR MR. PERRY: In response to your letter and under the Freedom of Information Act, we offer the following information:

During the period January 1, 1976, through May 31, 1980, our records indicate that SBA participated with the Arizona Bank in a total of seven loans to minority business persons, of which one was a black business person. Breakdown of these loans by year is as follows:

1976—1 loan	$42,000
1977—4 loans (1 black—$35,000)	205,000
1978—1 loan	220,000
1979—1 loan	52,500

We trust this is the information you desired.

Sincerely,

R. G. MORLEY,
Assistant District Director, Finance and Investment.

SMALL BUSINESS ADMINISTRATION,
Phoenix, Ariz., July 17, 1980.

Mr. MARVIN E. PERRY,
Vice President, The Arizona Center for Corporate Responsibility,
Phoenix, Ariz.

DEAR MR. PERRY: In response to your further inquiry, and under the Freedom of Information Act, please be advised as follows:

During the period January 1, 1976 through May 31, 1980, SBA participated with the Arizona Bank in 108 loans. Breakdown by year is listed below.

1976—32 loans	$3,411,140
1977—25 loans	3,426,000
1978—26 loans	3,744,500
1979—17 loans	2,825,700
1980— 8 loans	1,050,000

We trust this is the information required.

Sincerely,

R. G. MORLEY,
Assistant District Director, Finance and Investment.

U.S. DEPARTMENT OF AGRICULTURE,
FARMERS HOME ADMINISTRATION,
Washington, D.C., September 4, 1980.

Mr. MARVIN E. PERRY,
President, Perry Associates,
Phoenix, Ariz.

DEAR MR. PERRY: This is in response to your August 25, 1980, letter to our Arizona State Director regarding the loans guaranteed by our agency made through the Arizona Bank from January 1, 1976, to date.

The following is a listing of those loans:

Borrower	Amount	Date of guarantee
E & R Water Co	$300,000	3-30-78
Pile Enterprises II (Minority)	219,700	8-10-79
Cochise Vegetable Growers Association	150,000	8-15-79
Cochise Airlines, Inc	995,000	3-5-80

Sincerely,

JAMES E. BRYAN, Jr.,
Freedom of Information Officer.

PERRY ASSOCIATES,
Phoenix, Ariz., July 25, 1980.

BOARD OF DIRECTORS,
The Arizona Bank, 101 North First Avenue, Phoenix, Ariz.

DEAR BOARD MEMBER: I am appalled at the Arizona Bank's record of not lending to minority business persons in Arizona at the same time it was lending millions of dollars to South Africa. This rather shaky government has one of the world's worst human rights records.

During the period of 1976 to 1980 the Bank made millions of dollars available to South Africa with an approximate 68 percent Export-Import Bank guarantee. At the same time the Arizona Bank made only $519,500 available to minority business persons ($35,000 of which went to black business persons) under the Small Business Administration's 90 percent loan guarantee participation program.

From January 1, 1976 to May 31, 1980, the Bank made $14,457,340 in loans under the S.B.A. loan participation program. All minorities together received 3.59 percent of the total while blacks received 0.24 percent. Since approximately 4 percent of Arizona's population are blacks, proportionately they received only 0.06 percent of their parity share. This analysis does not take into consideration non-S.B.A. participation loans to businesses. If these figures were available, undoubtedly the disparity would be even greater. Additionally, the Bank's 1979 real estate loan disclosure statement shows a paucity of loans in South Phoenix's largely minority residential areas.

As an economist, it seems to me that if the Chairman of the Board, Mr. Tostenrud's, only interest is strengthening the state's economy, lending should start at home and then spread abroad. The state's economy would have benefited more from 90 percent S.B.A. guaranteed loans within the state than from 68 percent Ex-Im Bank guaranteed loans to South Africa. The benefit would be even greater if the loans went to local minority businesses, helping increase capital investments and decrease unemployment. The Board approved the Community Reinvestment Act Statement of the Arizona Bank. This is a beautiful document, on paper, what happened to its performance.

At a time when many banks in both the United States and abroad are reducing lending and denying credit to South Africa, and the South African government is fighting both internal and external liberation forces, a relatively small, state-chartered bank has eagerly made loans to that government. Why is the bank taking such a risk with their depositors' monies?

Were these loans to South Africa made out of sentiment or support for what that government espouses? This is a legitimate question considering the background.

After visiting South Africa, a former Chairman of the Board of the Bank championed the Ian Smith government's war against the freedom fighters. The timing of the start of the Ex-Im Bank loans intrigues me with the "coincidence" of two major events:

(a) The Soweto riots.

(b) Jeremy Shearer's (a high-ranking South African official) visit to the American Graduate School of International Management, whose Chairman of the Board, G. Clarke Bean, just happens to be Chairman Emeritus of the Arizona Bank.

In addition to the direct and indirect deposits of minority monies into the Arizona Bank, it should be remembered that minorities have also contributed to the Arizona Bank's well being through the purchase of stocks and bonds indirectly through I.E. Pension funds. Indicative is the fact that on June 30, 1979, Arizona State Retirement Fund held $850,000 of Arizona Bank notes.

As an external member of the Board of Directors, it is your responsibility to see that the Bank's management acts responsibly and in the best interests of both the shareholders and the community it was chartered to serve. Therefore, as a shareholder, I am requesting that you let me know where you stand on these matters.

I await your reply.

Sincerely,

MARVIN E. PERRY.

Enclosures.

[From the Phoenix Gazette, Aug. 12, 1980]

IN LENDING PRACTICES—BANK DENIES BIAS CHARGES

(By The Associated Press)

Charges of discriminating against minorities in its lending practices has been filed by a former employee against the Arizona Bank.

Marvin Perry, vice president of the Arizona Center for Corporate Responsibility, asked Monday that a federal agency investigate the bank.

In a letter to the Federal Deposit Insurance Corp., Perry charged that the bank "has failed to take an affirmative stance in real estate lending in areas predominately black and/or other minority. Under the Community Re-Investment Act of 1978, we are hereby requesting that the FDIC deny all present and future applications or request for branches, facilities, etc., by the Arizona Bank."

Arizona Bank President Robert Matthews denied all the allegations by Perry. He also said Perry had been fired by the bank.

"But for policy reasons I cannot say why," Matthews said of the firing. "We are under review by a regulatory agency as the result of a complaint filed by him."

Perry signed the letter as vice president of his organization, which he said will be applying for incorporation in September or October. The president is William Douglas, an economist and investment counselor from New York City, Perry said. Perry said he could not reveal the names of other members of the organization.

A spokesman at the FDIC acknowledged receiving Perry's letter and said it had been referred to the division of banking supervision in Washington and to the San Francisco regional office.

Among the particular charges Perry makes in his letter is that "from 1976 to 1980 the bank made millions of dollars available to South Africa with an approximate 68 percent Export-Import Bank guarantee. At the same time it made only $519,500 available to minority business persons ($35,000 of which went to black business persons) under the Small Business Administration's 90 percent loan guarantee participation program."

Perry also charged that the bank's SBA loan participation program shortchanged minorities; that the bank made a "paucity" of real estate loans in South Phoenix's largely minority residential area; and that the bank does not have a branch in that area.

Perry's request got conditional support from Darwin Aycock, secretary-treasurer of the Arizona State AFL-CIO.

Aycock said in a letter to the FDIC: "If the allegations in this document are true, and I have reasons to believe that they are, then I join in requesting that under the Community Re-Investment Act of 1978, that the FDIC deny all present and future applications or requests for branches, facilities and so forth by the Arizona Bank."

Specific information on lending is not available to the public because of privacy reasons, but "information we have internally would show we have loans to businesses far in excess of what he alleges," Matthews said.

Although Arizona Bank does not have a branch in South Phoenix, Matthews said, it is monitoring that area for a potential branch site.

"There are many other areas in the state where we do not have branch area, and we are monitoring them also," he added.

Matthews said the bank has heard nothing from the FDIC about Perry's letter.

NATIONAL BUSINESS LEAGUE,
Washington, D.C., August 15, 1980.

ROGER HOOD, Esq.,
Legal Division, Federal Deposit Insurance Corp., Washington, D.C.

Re: The Arizona Center for Corporate Responsibility

DEAR ATTORNEY HOOD: This letter is to express full, whole-hearted support for the position of the Arizona Center for Corporate Responsibility expressed in a recent letter to you with reference to practices of the Arizona Bank in Phoenix towards minorities in several areas of its operations.

We are especially concerned about the area of lending to minority businesses, not only the Small Business Administration's 90 percent loan guarantee participation program, but also the bank's regular loans to businesses. Our member-businesses and other organizations within the state have expressed their deep concern and frustration with availability of loan funds and capital generally for the blacks and other minorities in the business community.

The statistics furnished by the Small Business Administration to Arizona organizations interested in this problem, and relating to the SBA 90 percent loan guaranty program in conjunction with the Arizona Bank indicate only one (1) loan made to a black business during the period 1976 to 1980, among six (6) loans made to other minorities, and on hundred and one (101) loans made to majority citizens.

Our concern also extends to the area of real estate loans in the predominately black and other minority communities. The ability for black and minority businesses to survive and to succeed is in part influenced by a healthy, viable surrounding environment.

We look forward to an investigation of these charges by you within the near future.

Very truly yours,

THEODORE R. HAGANS, Jr., *President.*

ARIZONA STATE AFL-CIO,
Phoenix, Ariz., August 4, 1980.

Mr. ROGER HOOD, Esq.,
Legal Division, Federal Deposit Insurance Corp., Washington, D.C.

DEAR MR. HOOD: I am in receipt of a letter addressed to you dated July 29, 1980, and signed by Marvin E. Perry, Vice President, of the Arizona Center For Corporate Responsibility. I am also in receipt of a letter addressed to the Board of Directors of the Arizona Bank located in Phoenix, Arizona, dated July 25, 1980, also signed by Marvin E. Perry and two copies of letters from the Small Business Administration in Phoenix, Arizona, addressed to Marvin E. Perry and signed by R. G. Morley, Assistant District Director, Finance and Investment.

If the allegations contained in this documentation are true, and I have reasons to believe that they are, then I join in requesting that under the Community Re-Investment Act of 1978, that the F.D.I.C. deny on all present and future applications or request for branches, facilities and so-forth by the Arizona Bank.

I thought the time had long since passed when the Arizona Bank used discriminatory practices here in our community.

I would also like to be informed when your agency starts their investigation of these charges.

Sincerely,

DARWIN AYCOCK, *Secretary-Treasurer.*

NATIONAL MANAGEMENT SERVICES,
Phoenix, Ariz., August 14, 1980.

MARVIN PERRY,
Arizona Center for Corporate Responsibility, Phoenix, Ariz.

DEAR MARVIN: I received your letter regarding the low percentage of minority loans approved by the Arizona Bank.

As I mentioned to you, I was the Regional Director of the National Economic Development Association office in Phoenix for seven and one-half years. This company was funded by the government to assist minorities to start or expand their own businesses.

During those seven and one-half years we had over four hundred business loan approvals from banks and/or S.B.A., and I cannot recall any of those loans being made by the Arizona Bank.

I, therefore, personally support your efforts to get the Arizona Bank to participate more fully in S.B.A.-type business loans.

Sincerely,

RICHARD R. MEDINA, *President.*

November 6, 1979 — ARIZONA WEEKLY GAZETTE

Loans Limited In 'Poorer' Neighborhoods

Redlining

(Continued From Page A-1)

major repairs which are needed to bring the property up to par so the loan can be granted. Families don't have the money in their pocket to make the repairs to get the loans."

AS PORTILLO says, this is a "vicious circle". If the money for repairs is not loaned, the property can't be approved and if the property can't be approved, no money can be lent to buy it. In the end the family has to rent and the property in question continues to decline.

The Community Reinvestment Act was designed with the intention of correcting some of these problems, but neither the enforcers of the law, nor the banks, had any idea how this was to be done. The CRA was a nebulous, unspecific piece of legislation." John Gunther of the United States Conference of Mayors called the CRA's legislative mandate "without direct sanctions and with very indefinite requirements. The line between actions which are required and those which are merely encouraged by the statute and regulation is a fuzzy one."

SOMEHOW out of this confusion called the CRA, which went into effect a year ago last November, order is taking place. And where the various regulating institutions generally are lenient with the banks, they can get tough as a Brooklyn, New York savings bank found out when it was denied a bank branch because of a poor lending record.

The bite behind the CRA can be found in the regulations for compliance issued jointly by the four federal bank supervisory agencies (the Federal Deposit Insurance Corp., Federal Reserve Board, Comptroller Of The Currency, and Federal Home Loan Bank Board). These regulations instruct bank examiners to determine how conscientious the bank has been in meeting the needs of the local community.

The examiners must now include in their report such data as volume, geographic distribution of the banks real estate loan records and its efforts to market its credit services.

"These compilations of real estate loan data are, however, subject to interpretation and banks can avoid a charge of redlining if they have a few scattered loans in a deteriorating area. This then becomes more pink-lining than redlining and many Arizona banks fall into this pink zone."

THE FIRST National Bank of Arizona lent over $52 million in the Phoenix-Maricopa area for home mortgage loans and another $10 million for home improvement loans. In South Phoenix (Van Buren to Southern, 27th Ave. to 24th St.) they made nine home mortgage loans for less than $200,000 and 24 home improvement loans for $190,000. Robert Duckworth, executive vice president of the commercial banking group for First National said his bank was serving the needs of the community through all their loans. "But" he added, "we can't make loans to persons who don't request a loan. You don't force a loan down someone's throat."

"The lack of requests for loans in the South Phoenix area is the most common defense banks claim against charges of redlining. To a certain extent this is true. There is certainly not the volume of mortgage trade in South Phoenix that there is in the Mesa-Tempe area and the Black Canyon Highway area in north Phoenix, but it is also true that for a long time banks didn't market loans in South Phoenix and because some loan requests were, perhaps risky, they weren't accepted. No loan officer wants a failed loan on his record."

According to Joe Burkhart, vice president and manager of real estate loans for the Valley National Bank, the area is not very active for loans. Yet with 35 mortgage loans and 43 improvement loans it has the best loan record in South Phoenix.

"**THERE** is very little development in South and West Phoenix, but," he added, "it is a very good home improvement market and these are very good loans."

Western Savings, one of the largest savings and loan institutions serving Phoenix and Arizona also had a poor lending record in South Phoenix. In 1978, they gave out just six loans totaling less than $150,000.

Norm Miller, in-house counsel for Western Savings admitted that for a long time there was no bank activity in that area because the banks weren't marketing there.

THIS BECOMES obvious when looking at the number of banks south of downtown Phoenix. Only Valley National Bank and First National Bank offer full service banks. First Federal Savings has a branch and Western Savings has a branch in a Smitty's store.

The Smitty's Western Savings does not offer loans, but it does, as required by CRA, advertise the Western Savings' loan program. This type of small requirement should begin to change the face of loan patterns in places like South Phoenix. Western Savings, as are most of the major banking institutions in the state, is becoming progressively more involved in poorer urban areas.

This can be a result of recent CRA pressure or banks are finally realizing it may be a good investment to furnish home mortgage and home improvement loans in places like South Phoenix.

Almost all the major banks are involved with the Neighborhood Housing Services Program that targets certain areas for redevelopment. The Arizona Bank tried to develop a home rehabilitation program for the Chicanos Por La Causa organization. First Federal Savings is working with a number of urban groups such as the Phoenix Urban League and the Chamber of Commerce for South Phoenix and Western Savings now preaccepts a borrower for a home to be purchased at a later date.

BILL ARTHUR, of Arthur Associates, is rehabilitating a number of structures on Roosevelt Ave. just west of Central. He has sunk almost a quarter of a million dollars of his own money into the project because he was having such a difficult time getting money from the banks. Now some banks like Western Savings are beginning to finance him, but he says the problem has been trying to educate the banks to understand what kind of loans can be made safely in the Central-South Phoenix area.

He also says, that the banks should not be made out to be the only villains because the city shares a lot of the blame for money not being made available to South Phoenix. Antiquated laws make development difficult and costly, which in turn makes it hard for the banks to fund projects.

"The CRA isn't going to do it alone," he said referring to improving South and Central Phoenix through mortgage and improvement loans. "The banks are going to need the support of the city and the developers."

	MORT.LOANS	MOUNT	IMP.LOANS	AMOUNT
COMMERCIAL BANKS				
Valley National	35	965,000	42	249,000
[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
First National	9	186,000	24	201,000
H.S. Pickrell (United Bancorp)	4	344,000	7	8,000
SAVINGS AND LOANS				
Western Savings	6	144,000	0	0
First Federal	23	549,000	22	197,000

Table shows number and amount of mortgage loans and number and amount of home improvement loans by local lending institutions in South Phoenix area for period January 1978 through December 1978. Statistics for First Federal Savings are from January 1978 through June 1979.

EXPORT-IMPORT BANK OF THE UNITED STATES,
Washington, D.C., May 15, 1980.

Mr. MARVIN E. PERRY,
President, Perry Associates, Phoenix, Ariz.

DEAR MR. PERRY: This is in response to your letter of April 22, 1980, to Arthur Obester of Eximbank's Public Affairs Office requesting certain information on Eximbank guaranteed loans made by The Arizona Bank to buyers in South Africa.

According to Eximbank's records the following information is provided on The Arizona Bank's transactions for which an Exim guarantee was requested and approved. In all transactions The Arizona Bank was the applicant bank; Honeywell Inc., Phoenix, Arizona, was listed as the exporter for the computer systems; ESCOM of Johannesburg was listed as the obligor; and the Government of South Africa was the guarantor. Individual transaction details follow:

[Dollars in thousands]

Exim transaction number	Date approved	U.S. export value	Exim authorized amount	As of March 31, 1980		
				Amount cancelled	Amount disbursed	Outstanding
Gr-91-88	July 23, 1976	$930	$530	19	511	(1)
Gr-91-91	Sept. 28, 1976	618	421	90	330	(1)
Gr-91-92	Sept. 28, 1976	660	449	(2)	(2)	(2)
Gr-91-93	Feb. 16, 1977	750		(3)	(3)	(3)
Gr-91-94	Feb. 16, 1977	700	448	(2)	(2)	(2)

[1] Prepaid in January 1980.
[2] Exim commitment expired unutilized Jan. 31, 1980.
[3] Transaction cancelled.

Eximbank does not specify the rate of interest permitted to be charged by the U.S. commercial bank, but in the event of default, Exim's cover is limited to a maximum of 6 percent. The Export-Import Bank has not authorized any cover for U.S. export sales to South Africa since 1978 because at the present time Exim is precluded from doing so by Sec. 2(b)(8)[9] of the Export-Import Bank Act of 1945 as amended through November 10, 1978 (copy enclosed).

I trust that this provides all of the information you are seeking. I am sending a copy of this letter to Senator Dennis DeConcini of Arizona, whose staff inquired about the matter in your behalf, and to officials at The Arizona Bank, who also contacted us concerning the matter.

Sincerely,

NANCY S. PIGMAN,
Congressional Relations Officer.

Enclosure.

[From the American Banker, July 17, 1981]

ARIZONA BANK FACES SUIT, PROTEST

(By Gordon Matthews)

NEW YORK.—Arizona Bank in Phoenix is preparing to face allegations of racial job discrimination in federal court, as well as a protest campaign by a Phoenix consumer group.

The bank said it anticipates legal action after disagreeing with an administrative determination by the Equal Employment Opportunity Commission, which found "reasonable cause" to believe discriminatory job practices existed at the institution.

The Arizona Center for Corporate Responsibility termed the bank position "bad-faith action by an unenlightened management." The group promised protests, and anticipated a struggle like that by labor unions against J.P. Stevens & Co., the textile firm.

The group said it will urge depositors to boycott the bank, prod shareholders to divest stock, offer resolutions at the bank's annual meeting, organize demonstrations at bank offices and pressure other companies to remove bank officers as directors. One specific goal mentioned by the group was to have Visa International remove Don B. Tostenrud, the bank's chairman, from the bank card licensing organization's board of directors.

The EEOC alleged that the bank discriminated against blacks in job assignments, performance evaluations, promotions and salaries. The agency also said blacks were excluded from the "prestigious areas" of trusts, investments, and commercial and international banking.

The agency released its determination in a recent letter to Marvin E. Perry, a former managerial trainee at the bank and now president of the Arizona Center for Corporate Responsibility.

According to the commission's documents, the bank terminated Mr. Perry, who is black, for "unsatisfactory" job performance. The EEOC noted that after Mr. Perry was employed at Arizona Bank, he engaged in civil rights protests at shareholder meetings, press conferences and to government agencies.

In his 26 months of employment at the bank, Mr. Perry was rotated through 17 different work assignments, the commission said. By contrast, similar nonblack employees received no more than four assignments in 15 months.

The bank asserted this was done to facilitate Mr. Perry's success. The EEOC countered that it found no evidence the moves were to advance his career. Rather, the moves often seemed to be "punitive in nature," it said.

Arizona Bank released the following statement about the EEOC action:

"The EEOC has made an administrative determination in the Marvin Perry case which is not favorable to the bank. The bank disagrees with that determination and does not believe there is a factual basis for it.

"We are proud of the bank's employee practices and policies and believe that no bank employee has suffered discrimination.

"Litigation may soon follow, and in that event we look forward to the opportunity to present the bank's case in federal court with confidence that our employment policies and practices will be found to be in full compliance with the law.

[From the Arizona Business Gazette, Apr. 7, 1981]

FORMER EMPLOYEE CLAIMS HARASSMENT BY ARIZONA BANK IN BAD DEBT SQUABBLE

(By J. Craig Coulombe)

What happens when you get on the wrong side of a bank?

What happens when you believe serious inequities exist within the state's third largest commercial banking institution and you go public with the story and raise charges against the bank with the Equal Employment Opportunity Commission (EEOC) and the National Labor Relations Board (NLRB)?

What happens when you lose your job afterwards and can't get steady employment?

Answer: Plenty—especially when you still owe that bank money.

Marvin Perry owes Arizona Bank $675.92, plus 7.98 percent interest accrued from January 1979 to September 1980, on his VISA credit card account which he says he voluntarily closed after he was fired by the bank Sept. 22, 1978. Perry said he cut the card in two and left it on his boss' desk two days later.

Perry worked for Arizona Bank for almost two years as a branch loan officer class three, a position with a payscale ranging from $17,000 to $26,000. Although the bank gives its officers special commercial VISA cards for business purposes, Perry said his account was a personal one with a $1,000 monthly limit and a special lower monthly interest rate the bank gives its employees.

"That's one of the problems," Perry said. "When I applied for the card, I asked for the $1,000 limit, but Arizona Bank only gave me a $500 limit without explaining why I wasn't given the requested amount.

"The bank in effect violated the Equal Credit Opportunity Act, a federal law, that specifies that when one requests a loan and the terms of that loan are substantially altered, the loaner must give a detailed, written reason why," he explained. "The bank did not do that and they face a $10,000 fine which could make the loan null and void.

"So technically, I don't owe the bank anything, but I want to honor any debt."

After he was fired, Perry said he made several payments to The Arizona Bank, but due to lack of steady employment and lack of steady revenue, he had to stop paying. He said he has paid $200 on his loan.

On Dec. 5, 1980, the Arizona Bank filed a suit in Maricopa County Superior Court against Perry to collect $675.92 plus 7.98 percent interest from Jan. 3, 1979 to Sept. 15, 1980, as well as the bank's costs of $151.55, attorney John W. Wall's fees of $350, "reasonable attorney's fees after settlement," and interests on all costs and fees at a rate of 10 percent a year from judgment.

Perry wrote the first of six letters to Wall requesting an out-of-court settlement, saying "evidently, my loan is an active and open account," despite his belief that the account was closed. The bank refused to respond.

According to superior court files, Perry offered, in a letter to Wall dated July 14, 1980, to pay Arizona Bank $10 a month until the loan was paid off. The next day he upped the offer to $20 a month.

On Feb. 25, 1981, Arizona Bank sought a supplemental proceedings order from Court Commissioner John Trombino demanding that Perry appear in court and produce all records relating to property, income, business transactions, purchases or sales of Perry's property or assignments or transfer of property by him on or after Jan. 1, 1976.

The order demanded that Perry produce the following material:

"Titles, deeds, mortgages, assignments, bank statements, financial statements, bank books, check books, checks, check stubs, cancelled checks, deposit slips, passbooks.

"Documents of sale or lease, documents of assignments, bonds, stock certificates, loan documents.

"Boat or aircraft or vehicle registrations and titles, bills of purchase or sale, records of accounts receivable, books of accounts, federal and state income tax returns for calendar years 1976 to date and other documents relating to matters above."

The order defined "records"—without limitation as "every writing of every type or description, and every instrument or device by which, through which or in or on which information has been recorded or preserved, including but not limited to:

"Memoranda, notes, letters, books, records, worksheets, drawings, graphs, charts, maps, film, photographs, handwritten notes, logs, video, wire or tape recordings, phonograph records.

"Computer cards, tapes and printouts and other data compilations from which information can be obtained. The term 'records' also means every copy of a record where such copy is not an identical duplicate of the original."

Perry said he would need a truck to haul all the material requested to the courtroom and that even if he did, the bank could claim that he was withholding something and file contempt charges against him.

Chief Presiding Judge Robert C. Broomfield of the superior court apparently felt the order was too imposing and on March 5 squashed the bank's supplemental proceedings because such a demand presented entrapment.

Perry said the bank also requested "body attachments" twice which would mean his detainment by county sheriffs for Perry's failure to appear at the Feb. 25 hearing. Both motions were also quashed by Broomfield on March 6 and March 10.

Recently The Arizona Bank submitted a *precipe duces picem*—a request for a subpoena of documents—in superior court for Perry. Perry said he will file for a dismissal of the order with prejudice in the court to make sure The Arizona Bank cannot appeal to the state Court of Appeals.

Because The Arizona Bank has rejected Perry's suggested payments and instituted such harsh legal measures, it appears as if the bank is going out of its way to collect on this account. The question is why?

Perry says he is certain that the bank is retaliating against him for complaining to EEOC and NLRB and this suit for collection is a form of harassment.

According to an article in the *Arizona Weekly Gazette,* dated Sept. 9, 1980, Perry, besides filing EEOC and Department of Labor discrimination suits, as an Arizona Bank shareholder, also sought to include minority hiring data on the bank's annual shareholder's reports, a request for resolution to include:

Employment data for the last four years listing the total number of males and females in each of the nine standard categories and the separate listing of the number of minority females in each group.

Summary of the bank's affirmative action program with goals and guidelines.

Evidence showing the bank's appraisal system has not abridged promotional and employment opportunities of blacks and other minorities.

A summary and detailed status report of all complaints filed during the last four years with EEOC or other official agency or court, including a breakdown of the yearly amount spent on each complaint and assessment of potential damages.

The Arizona Bank fought these requests until February 1980 when the bank and Perry reached a compromise in which Perry agreed to drop part of his demands and the bank in turn agreed to publish in its 1980–83 inclusive Annual Report To Shareholders several of Perry's proposals.

The bank has consistently denied all discrimination charges.

Hank Berry, a senior vice president of the bank, said the bank could not comment on Perry's charges of harassment, because answers to the allegations were in a sealed statement with the state Superintendent of Banks.

Roy Schuetze, banking division supervisor of the Superintendent of Banks, confirmed that Arizona Bank's response had been filed with his office and Arizona Revised Statutes section 6-129 prohibits public disclosure of such documents.

Valley National Bank and First National Bank of Arizona said their criteria for collection procedures depends upon each individual case—and would not specify what that criteria precisely is.

Each bank, however, emphasized that if an individual has a former history of good credit and attempts to work with the bank, they will give him every opportunity to repay them and rarely will use litigation to collect in such a situation.

Perry said until he fell behind in his VISA payments, his credit rating was excellent.

As a former loan officer, Perry also said he understands how the bank generally deals with delinquent accounts. He outlined the process as such:

The Arizona Bank's VISA department will send a form letter to a customer who is 60 days late in paying his account and after 90 days, the bank will close the account.

Between 60 and 90 days after failure to pay the account, the bank will make telephone calls to the customer requesting a plan for payments.

After 120 days, the account is referred to the bank's adjustments department which handles collections. The adjustment department will call the customer and attempt to set up a payment plan that the customer can handle.

If the adjustment department determines that the customer cannot pay anything on the account, it will usually write it off as a bad debt.

If the bank pursues collection of a debt, after six months, the adjustment department will send a "demand" letter if the bank thinks the customer has money and is holding out on paying.

After eight months, the bank's attorney will send a letter giving the customer two weeks to make payments. Usually after another two weeks, the attorney will file suit for collection in the justice court.

Once the bank has filed for collection in the court, the bank's attorney will order the customer to his office for interrogatories or to give the customer one last offer for reduced payments, Perry said.

"The bank figures that some money is better than no money and they will try to collect whatever they can and write off the rest as a loss," he added.

If the case goes to court and the facts show that the customer is working, the bank may attempt to garnish his wages, Perry said.

"There are two keys to this case," he said. "First, the bank would not want to spend as much money as they are just to collect a $676 account, and second, the bank generally will accept $8, $10, or $20 a month to pay off an account."

Perry also accused the bank's process servers, Hawkins and Campbell, Inc., 914 W. Madison, Phoenix, of harassing him at all hours on the telephone and has filed a complaint about the company with Maricopa County Superior Court.

He described the bank's tactics as an infringement on his civil rights and liberties and called this a case of "unwarranted invasion of privacy."

[From the Arizona Republic, March 1980]

ARIZONA BANK ASSAILED FOR LOANS TO SOUTH AFRICA

(By Dan McGowan)

At first glance, Arizona would seem to have little to do with the Republic of South Africa, a remote nation on Africa's tip known for its gold production and its system of legal racial discrimination called "apartheid."

But distances are short in the world of international finance, and South Africa, wealthy and sharing many of America's values, is attractive to many U.S. companies.

One company attracted to South Africa was the Arizona Bank, and its involvement sparked a controversy that led to a stockholder's calling for Chairman Don Tostenrud's resignation. Although the shareholder and others believe lending to South Africa is morally wrong, the bank defends its activity as good business and helpful to Arizona's economy.

In 1978 and 1979, Arizona Bank loaned slightly more than $1 million to South Africa's major utility, the Electricity Supply Commission, or Escom. The utility used the loan to buy Honeywell computers for two new powerplants outside Johannesburg, its headquarters city.

Between June 1976 and February 1978, the bank also was prepared to advance Escom more than $1.1 million in additional credit, bank officials have acknowledged.

Bank records made available to the Arizona Republic show that Escom borrowed a total of $1,051,806, repaying the amount in three installments. The final payment was sent Jan. 14, records show.

Tostenrud says his company has no more dealings with any public or private institution in the Republic of South Africa.

In April, Arizona Bank stockholder Marvin Perry claimed the bank had tried to cover up its dealings with South Africa and has called for Tostenrud's resignation.

Although it's difficult to pin down the extent of U.S. bank lending to South Africa, it would appear the amount is large. Stockholders of several banks have estimated that in 1976, U.S. banks advanced $750 million to agencies or companies in South Africa.

South Africa's racial policies have prompted lobbying against bank loans to that nation in some parts of the United States.

An executive for the U.S. Export-Import Bank, which guarantees loans made by U.S. companies to foreign countries, believes the Arizona Bank loan to Escom was small compared with the overall flow of American money to Johannesburg.

"It represents a very small percentage of total (money) flow to South Africa and a small percentage of loans to Escom, I would think," said the executive, who asked to remain unidentified. "Escom is a very large utility that buys a lot of equipment from the U.S. . . . My feeling is that Escom would consider this a medium-sized purchase."

However, opponents of South Africa's system of segregation believe any lending activity helps prop up Johannesburg's apartheid policies.

According to Dumisani Kumalo, leader of the New York-based Campaign to Oppose Bank Loans to South Africa, "It has been proven beyond doubt that every loan that has been made to South Africa has gone to strengthen apartheid. There is not a single loan that has gone to benefit a black person."

Kumalo, a black former South African journalist, said electricity and telephone service are reserved for whites and are rarely provided for black South Africans.

"In 1967, I applied for a telephone, and when I left the country 10 years later, I was still waiting," Kumalo said. "I gave up on trying to get electricity."

Tostenrud says helping Arizona was the bank's main consideration in making the loan to Escom.

"Everyone has their own views," Tostenrud said. "We try to conduct the bank's business according to the credit worthiness of the applicant, the soundness of the loan, what it's doing in the state of Arizona, and leave the political considerations out of it.

"It (the loan) provided jobs for Arizona. . . . Our main consideration simply was providing the financing for a manufacturer based in Arizona.

"We made no other loans to South Africa other than this one," he said.

Tostenrud would not say whether the bank would again lend to a South African company or government agency.

"Since it's not a question that's been put to us, I just don't really have any comment."

Economists estimate that $1 million will fund 40 full-time jobs for one year. Presumably, the loan to Escom provided that amount of jobs for Arizona

The computers were purchased from Honeywell's large information-systems division in Phoenix.

Records provided by Arizona Bank and confirmed by the Export-Import Bank in Washington show that the Phoenix bank's relationship with Escom began in June 1976. At that time, Arizona Bank made a loan commitment of $550,000 and the Export-Import Bank agreed to guarantee it. Eventually, the commitment was increased to $927,775, and on July 5, 1978, Arizona Bank lent Escom $638,751 at 10½ percent interest.

Concurrent with these actions, the bank made a second commitment of $618,750, and Export-Import approved it Oct. 19, 1976. This commitment was revised twice and stood at $635,979 on Jan. 18, 1979, when Escom borrowed $413,055 on it at an interest rate of 13¼ percent.

As these two actions were being taken, Arizona Bank made a third loan commitment of $660,000, which Export-Import approved Oct. 19, 1976. None of this money was borrowed.

Altogether, the bank made a total of $2,223,754 in advance commitments to Escom. Although the utility borrowed a little more than $1 million, its maximum loan balance was $945,348.

Escom made three payments on the loan in 1979 and last January retired it with two lump-sum payments totaling $770,046. Escom told the bank it was doing this because of high American interest rates and because the utility had a strong cash position.

"It is our sincere wish that we may at some future time have the opportunity of furthering what has been a most pleasant relationship," Escom told the bank in a letter.

Mr. MITCHELL. Our next witness is Mr. Robert Kline, director, support operations staff, Government Electronics Division, Motorola, Inc.

It has been a long day. You have been very patient in waiting to testify. We thank you for your patience.

We have a copy of your testimony. You can submit it in its entirety for the record and speak to the high points, or you can read it. The option is entirely up to you.

TESTIMONY OF ROBERT F. KLINE, DIRECTOR, SUPPORT OPERATIONS STAFF, GOVERNMENT ELECTRONICS DIVISION, MOTOROLA, INC.

Mr. KLINE. I would prefer submitting it for the record. I will just pick pertinent sections out.

Mr. MITCHELL. Without objection, the entire testimony is submitted for the record.

Mr. KLINE. To members of the Committee on Small Business, and Chairman Mitchell, I would like to welcome you to Phoenix. My name is Robert Kline, and I am employed by Motorola, Inc., in its Government Electronics Division, headquartered nearby in Scottsdale.

I have a new title since preparation of the written testimony—director, support operations staff. In this role I have responsibility for procurement and many other related functions.

We at Motorola thank you for your invitation to testify today. We are proud of our record in support of the small and small disadvantaged business communities and of our record of compliance with Public Law 95-507.

Today, although we have other Motorola activities in the local area, as well as worldwide, I am going to be speaking primarily to the activities of the Government Electronics Division.

While these other parts of Motorola do make some sales to the Government, our division, which I will refer to as the GED, sells principally to government entities. We represent approximately 10 percent of total Motorola activity nationwide, worldwide.

Our primary customers are the Department of Defense, the National Aeronautics and Space Administration, the National Security Agency, and the many large prime contractors throughout the country who serve these agencies.

We are not totally a prime contractor. We are often a second- or even third-tier subcontractor.

Our total employment at this time is approaching 6,000. We now occupy several plant sites in this area. We spend one-half of our procurement dollars with small businesses. I might add this is a long-time figure.

I am now in my 24th year at this division of Motorola. We have always spent about half of all of our dollars for goods and services with small businesses.

Of this amount that we spend with small business, at this time about 6 percent is spent with small, disadvantaged business. This 6 percent has grown from 2 percent 5 years ago. We believe that Public Law 95-507 has been a factor in this growth.

I would point out that we had, prior to the enactment, and the preenactment activities, prior to Public Law 95-507 being passed, we considered ourselves an affirmative action contractor. Yet, nevertheless the enactment of the law has provided the motivation to triple our small business involvement in these past several years. We hope it is going to still go higher.

One of the actions that we have taken or that are ongoing in our compliance with the public law is that we moved right out and provided a small and small disadvantaged administrator—Buddy Perez. He is sitting in the back of the room.

We are very proud and pleased to have Buddy as part of our staff. Buddy, would you rise. You can't miss Buddy.

Mr. MITCHELL. Fine. We need someone like him for the Office of Small and Disadvantaged Businesses, somebody big enough to have impact.

Mr. KLINE. That is right. Buddy has a lot of clout. To be serious about it, Buddy knows everybody there is to know in this community. He is the entry person for any small business that wants to do business with Motorola, Government Electronics Division. He sees to it that they get established and know the buyers and so forth.

Many of the things that I am going to mention here are Buddy's doing. He is the prime mover in making some of these things happen.

We are very proud of being a subscriber to the PASS system mentioned here in earlier testimony. We were the first PASS subscriber in the State of Arizona, I might add. We are very pleased and honored that Tom Trimbol awarded us a plaque in honor of our being the first industry in Arizona to subscribe to that very good system. Buddy was a prime mover in us doing that.

We host a lot of minifairs at our plant. We have a very nice set of meeting rooms and facilities. We open those facilities up to small suppliers who want to come in and need a place to meet. We let them then show their wares, to not just us, but to other industries in the area. We publicize these fairs.

We participate in many minority trade fairs throughout the country. I have told Buddy, "I want you to budget for at least four times a year to travel and take a booth and take literature to these trade fairs that occur throughout the country."

We have a continuing buyer training session to maintain an awareness of our obligations under the public law. This is ongoing.

We assist suppliers with technical skill training in their plants and in our plant. We help them with paperwork, with bidding procedures. We have helped small suppliers get better pricing from their suppliers at times when that is a problem.

We are involved in community activities. Our buyers participate as members of the Arizona Minority Supplier Development Council. Our company provides the public relations assistance to that council.

We feel that we are also—and I won't list them all; you people are more familiar than we—in compliance with the many requirements of Public Law 95-507. We hope and feel we are complying with all of them.

We must point out to you that we are very proud of the fact that our name is not on the list that was provided by the SBA to you people in Congress as part of the law, people who have been found to have subcontracting plans that in the judgment of the SBA maybe are not up to snuff. We are not on that list. We hope we will never be on that list.

In addition to these things that we are doing that are ongoing, we would like to mention two specific examples of our commitment.

First, we took a look at a unique situation. For those of you unfamiliar with this area, on the eastern side of Scottsdale everything stops as though you drew a line with a ruler. It is because an Indian reservation starts there, the Salt River Pima/Maricopa Indian community.

While they have not been mentioned here today in any previous testimony that I remember, the American Indian is a bona fide minority on the SBA list of qualified minorities.

We needed a warehouse. We found ourselves constantly in need of more space than we had. So we approached these people in this Indian community. To make a long story short, with their money, they built a warehouse to our specs. We now lease it from them.

The lease represents quite a bit of money that that is on the right side of the ledger as far as our minority business buying is concerned. The situation has worked so well that the Indian tribe is now working deals like it, or starting to, with other people.

Another example, and one that will lead me to a problem. We were approached by a minority small travel agency asking for some of our business. It created kind of a dilemma. We had a travel agency, a small business, not a minority small business. We were very happy with that travel agency. It has been serving us well. However, we did earmark a piece of our business for the minority travel agency, and they still have it now.

I would like to use that example to point out what we view as several problems in our attempts to live to both the letter and the spirit of Public Law 95-507.

I am going to cite three areas that would seem to be major causes of friction and frustration for ourselves and for the prospective small business suppliers that come and call on us.

I don't expect you folks on the committee to have any answers. I want to cite these problems. I am not really seeking sympathy, but I want you to understand that even for those of us trying very hard to be good citizens under this law, there are compelling things that get in the way at times.

The first problem is the one that does underlie my travel agency example. What do we say in a case where we have an existing supplier? He has not done a thing wrong. I shouldn't say he. It might be a she. The supplier has not done anything wrong, he is a successful supplier, the price is right.

Now comes a new person entering the scene--small, large, minority, majority, whoever. What is our posture when everything else is equal in taking away some business from the guy who hasn't done anything wrong.

In the case of the travel agency, I have to say that I did. I took some business away. I gave it to the new minority travel agency. But gee, with 75 buyers who I cannot be holding hands with every moment—and these buyers interfacing all day, every day, with whoever happens to be coming in our door, I submit that it is very difficult to establish an equitable guideline for those kinds of situations.

I can understand people who maybe have called on us and were not successful and now are bitter. I can fully understand them. Yet we are facing a dilemma of sorts as well.

Another problem occurs, and this occurs more often than you might realize, when a small business in attempting to compete cannot quote as low a price as a larger business—and I am not now talking large business, I am talking larger business—because his buying power from the basic manufacturer isn't great enough to get the same price advantages.

We have helped a few of those cases. We have leaned a little bit. We cannot help them all. We have had some sad situations where we were unable to buy from the company that had the higher price.

As you gentlemen understand, there is nothing in the regulations that relieves me when the Government auditor is in there going over how we are doing in our business and sees that I have paid more than I needed to in a certain situation. There is no relief for that in law today.

A third problem involves end item product qualification. Simply stated, in our work at any rate, this means once a product, say a radio, has been qualified—you understand I am now not talking in the civilian arena, but I am talking in Government merchandise where qualification is something that is big. It means that this thing, say this microphone, when it first got built and first got designed passed a very stringent set of specifications and tests in order that it meet the Government specifications and remain a good product and work on a battlefield or wherever.

When things get qualified, from then on that must be it. This little switch on the front here, if I got a new guy coming in saying, "Hey, I want you to use my switch"—2 or 3 years later—I cannot do that without a complete requalification of that whole microphone.

Most often the Government customer who wanted that microphone does not want to pay for new tests. He wants the microphone just like it was. So I say that time hopefully may or will cure this problem in that since we have the public law, the smaller and small disadvantaged suppliers are getting, not just from us but nationwide, more opportunities to bid.

So as time passes, those folks will have their parts in the next version that is going tc get qualified. It is going to be I think a self-cure. But right now, it is a frustrating thing for both of us.

Before closing, I want to mention an administrative concern. You know it is September 1 today. In just a little more than a month we will hit the third anniversary of Public Law 95-507.

From our side, defense contractor's side, it is almost a travesty, the time it has taken to bed down a mutually acceptable set of reporting forms and reporting criteria on how we are doing against the public law.

The forms that we have today are still up for discussion. They are not the final version.

I just read this past week an industry association letter that is going to the Government, still in the ongoing dialog about the format of these reporting firms. That is 3 years since we have had the law.

Now, we are concerned about the reporting requirement, the contract-by-contractor reporting requirement. In my plant, we are what is called an electronics job shop. A job shop in the trade parlance is a shop that is building a myriad of products, not just a single product. We probably have 250 to 300 active contracts.

Now, since the public law came in, and assuming it meets the dollar threshold, each and every contract now gets separately monitored and reported on as to progress against the goals that were stated in its subcontracting plan—a massive computer programing task that has been made doubly difficult because the forms themselves have been so fluid.

They have gone through at least four iterations in 3 years in an attempt to get forms that are usable. So, we still do not have a good set of instructions to issue our computer programers as to how to even do this.

A lot of us feel that the same end result could be accomplished if we could report collectively—collect on a weighted basis the goals and actuals from the many contracts we are working under and report on one large set of dollar numbers instead of each and every contract.

Now, I have had an alternative mentioned to me that kind of ties back to that SBA scoresheet. It is kind of traditional—that I use in my prepared statement—an analogy to the quality profession, where the better your historic quality, the less you get inspected.

I draw that analogy here. I could use one that might even be closer at hand. The procurement system review part of the DARS, where if your procurement system is reviewed by the Government and found OK, you then don't have to run to the contracting officer for lots of other approvals along the way.

That might be a little nearer at hand even than my quality analogy. I am just saying there may be a way for those people that are found in compliance, for the burden of review or audit to be relieved.

With that, gentlemen, I thank you for this opportunity today.

[Mr. Kline's prepared statement follows:]

Prepared Statement of Robert F. Kline, Director, Support Operations Staff, Motorola, Inc., Government Electronics Division, Scottsdale, Ariz.

To members of the Committee on Small Business and Chairman Mitchell, I'd like to welcome you to Phoenix. My name is Robert Kline and I am employed by Motorola Incorporated in its Government Electronics Division, headquartered nearby in Scottsdale. My title is Director, Support Operations Staff. In this role I have responsibility for procurement and related functions.

We at Motorola thank you for your invitation to testify today. We are proud of our record of support to the small and disadvantaged business communities and of our record of compliance with Public Law 95-507.

First, I believe we must set the scene for you as to just who we are. For many, Motorola is almost a household word. We are a global company with over 70,000 people worldwide. Our specialty is electronics—all the way from the basic components such as transistors, integrated circuits and microprocessors to the two-way radios you see in taxis and trucks; the pocket beepers your doctor has; your auto radio; the new computerized auto ignition systems; mobile telephones; and very sophisticated items for defense and aerospace uses. I'm sure I have left out a great deal, and apologize to my Motorola colleagues if I have slighted anyone, but I simply wanted to give you a general picture.

Of the many Motorola activities and operations, two are headquartered here in the greater Phoenix area. One of these, and a very large one indeed, is our Semiconductor Sector. This Sector of the company contains the groups and divisions that manufacture semiconductor devices—the dynamic building blocks for most electronics. This part of our company is a procurer of basic raw materials that are made into these components that in turn are incorporated by others into the more familiar end items of electronic equipment.

This brings us then to the other Phoenix area activity—Motorola's Government Electronics Division. I will be speaking today primarily of the activities of this division. While the other parts of Motorola make some sales to the government, our division, which we will refer to from here on as GED, sells principally to government entities.

GED represents 8-10 percent of total Motorola activity. Our primary customers are the Department of Defense (DoD), the National Aeronautics and Space Agency (NASA), the National Security Agency (NSA) and the many large prime contractors who serve these agencies.

This division of the company has been here in the Phoenix area about 30 years, but of course Motorola's history of defense electronic production goes back to World War II. Some of you probably remember our Walkie-Talkies of that era.

Total GED employment is approaching 6000 and we now occupy several plant sites in this area.

From a statistical standpoint, and finally getting around to matters of interest to your committee, we spend one-half of our procurement dollars with small businesses. Of the amount spent with small business, about 6 percent is spent with small disadvantaged businesses. This 6 percent has grown from 2 percent five years ago, and we believe that Public Law 95-507 has been a factor in this growth.

Here are some of the actions we have taken or that are ongoing in our compliance with Public Law 95-507.

1. SMALL/SMALL DISADVANTAGED ADMINISTRATOR

Diego "Buddy" Perez is our administrator. We are so very fortunate to have him in this position. I can truly say that everyone knows Buddy—both in the GED and in the community. Buddy works ceaselessly to bring together our buyers and the small/small disadvantaged suppliers. Buddy is also the driving force behind many of the items to follow.

2. PASS SYSTEM

PASS—Procurement Automated Source System—is the computerized listing of small/small disadvantaged suppliers maintained by the SBA. Motorola GED was the first PASS subscriber in the state of Arizona and was publicly honored for this by the local SBA Director. We hosted a demonstration of the PASS System for over 100 representatives of other state industries, small businesses and government agencies.

3. MINI-FAIRS

We host MINI-FAIRS where we open our meeting room facilities to small/small disadvantaged suppliers so that they can interface with our buyers and buyers from other local industries.

4. TRADE FAIRS

We participate in minority trade fairs, sending procurement representatives to man booths and talk to prospective suppliers.

5. BUYER TRAINING

We have continuing buyer training sessions to constantly maintain an awareness of Public Law 95-507 obligations. These are conducted by both our own management people and by guest instructors from SBA and other professional groups.

6. ASSISTANCE TO SUPPLIERS

We have assisted suppliers by conducting technical skill training in their plants, helped in paperwork and bidding procedures and worked with them in getting better pricing from their suppliers.

7. COMMUNITY INVOLVEMENT

Several of our buyers have actively participated as members of the Arizona Minority Supplier Development Council. We also have provided public relations assistance to the Council for several years.

We also are complying with the detailed administrative provisions of Public Law 95-507. We note with some pride that the SBA Annual Report on Federal Agency Subcontracting Plans for fiscal year 1980 which was recently submitted, as required by law, to your Committee and to the Senate Select Committee on Small Business does not contain our name. As you know, the SBA Report includes a lengthy list of contractors whose subcontracting plans were found not to contain maximum practicable opportunities for small and small disadvantaged business to participate in contract performance.

In addition to these continuing efforts or actions, we would like to mention two specific examples of our commitment. First, we looked at a unique situation wherein we are located very near the Salt River/Pima-Maricopa Indian Community. We proposed and they accepted a plan whereby they built and leased back to us a warehouse on Reservation land. This situation worked out so well that the Indian Community now has several similar developments underway with others.

In the second example, we were approached by a minority travel agency for some of our business. Now, our travel needs were being very well taken care of by another small non-minority business. Nevertheless, we gave a portion of the business to the minority travel agency. We could go on with other examples of special help or effort to aid small businesses both minority and majority, but we would prefer to use this travel agency example to point out what we view as some chronic problems in our attempts to live both to the letter and the spirit of Public Law 95-507.

We will cite three problem areas that seem to be major causes of friction and frustration for ourselves and prospective small suppliers. We don't expect you to have the answers, but want you to know that these problems exist and plague even those of us who are trying to do our best under the Law.

The first problem is the one underlying the travel agency example. What is the answer when an existing supplier—who may be large, small, majority or minority—is serving you well and a new small or small disadvantaged supplier wants "a piece of the action?" (Assume that price and service are equal.) This, gentlemen, is a recurring problem and one that is most difficult to explain and establish guidelines for buyers to follow. As we're sure you can see, someone is upset whatever we do.

Another problem occurs when a small business cannot compete because his buying power is not as great as that of his larger competitors. We see this happen every day and there is not much we can do. As you gentlemen know, we, as a prime or lower tier major subcontractor, are under continual audit or review and there are no provisions in the regulations to allow paying higher prices to small businesses.

A third problem involves end item product qualification. Simply stated, this means that once a product—say a radio—has been qualified, then it must be built in the as-qualified configuration from then on, or else undergo very expensive requalification tests. Many products have a long re-procurement life and we are constrained to continue to manufacture them as they were originally qualified, thereby limiting opportunity for new suppliers of their components. Time may cure this problem as newer products take over—products that are designed and qualified during the Public Law 95-507 era where more opportunity to get "designed-in" exists for more suppliers. Meanwhile, it does add to our frustration.

Before closing, we will also mention that there is an administrative concern we and others have about the reporting requirements under Public Law 95-507. Contract-by-contract reporting is a burden for most of us and is a significant increase over previous reporting requirements. Perhaps a less onerous reporting method could be found—at least for those contractors found by the SBA to be in compliance.

There is a precedence, of sorts, for this in the quality area where the better your quality, the less the inspection.

We thank you for this opportunity today.

Mr. MITCHELL. I thank you for your very interesting testimony.

Certainly, we should not always criticize. We ought to commend when a real positive effort is being made. You have increased your minority business procurement dollar up to 6 percent. You indicated that you hoped it would go beyond that. I think that is good. I think one of the ways you will get it beyond that is to set definitive goals each year.

Mr. KLINE. That is correct.

Mr. MITCHELL. I have never known any program to succeed that did not say this is the goal for this year, the goal for next year, the ultimate goal. I just assumed you would be doing that.

In addition to that, I am sympathetic with your frustrations about the reporting system, but I hope you can be sympathetic with my frustrations. After being in this business of economic development, small business, minority business, for more than 10 years, one of the things that has given me the most trouble has been the adroitness, for lack of a better word, with which many companies will report in to the Government in terms of compliance, and then when we take a deeper look, there really is not compliance. There is a masked over kind of operation that purports to be compliance.

I wish that all the companies would have the same good reputation that you have and would try to aspire toward compliance, such as you have. But they don't. That is my dilemma. How do we resolve the problem of not overburdening you, and yet at the same time ascertain full compliance with the law?

By way of illustration, you deal with 300 companies, smaller contracting operations.

Mr. KLINE. We have 300 contracts. We are dealing with thousands of suppliers.

Mr. MITCHELL. OK. The 300 contracts. It is quite possible—and I know this has not happened in your case—that that increase in the minority business dollar, you could attribute to only 100 of the 300 companies. That is quite possible, which means you are being unfair really by permitting the other 200 companies to get off the hook and 100 companies carry the weight for them.

These are some of the frustrations and some of the problems that we have to confront. I don't want to just dismiss this saying, well, there is not much we can do about it.

I think we need to give it serious thought. I certainly intend to do that as chairman of this committee. I am certain my colleagues will do the same thing. But it is a lot of real commitment on the part of most companies to comply with the law, which almost creates some of the problems that you allude to.

I don't know how to answer your—maybe I might. Motorola is doing well, business is good?

Mr. KLINE. It is all right.

Mr. MITCHELL. Profits are high?

Mr. KLINE. I am going to be very frank with you. They are not in our sector. I am not going to get into a discussion of Motorola overall. I don't have the right to do that.

Mr. MITCHELL. Of course not.

Mr. KLINE. But I do want to say that in our sector that serves the Government, we have had a couple of pretty bad years. I will make that statement to you.

Mr. MITCHELL. All right. But then even during that period you found the need for some expansion, the plant on the Indian reservation.

Mr. KLINE. Right.

Mr. MITCHELL. I would assume those couple of bad years will quickly be dissipated and future years will be very good. I think that is one of the means by which you address the problem, the dilemma you confronted, with reference to your travel agency.

As new opportunities open—believe me, I am fully aware of the institutionalized practices in the private sector. "This is Joe. I dealt with his father, and I expect to deal with his son. We have been doing it for 30 years. Why change?"

One of the ways to avoid that is that as you see new opportunities, it seems to me that priority ought to be given to those who have not been included in the operation, just as you did with your work on the Indian reservation.

Also let me say this. I am always overawed by the genius of the American private sector. That genius is going to find a way of doing this.

Mr. KLINE. I am sure it will.

Mr. MITCHELL. Sure it will. We don't even have to worry the Congress with that, do we? You will find a way. I have seen the technological genius of America almost perform miracles. Surely that genius will be able to find a way to come into full compliance with Public Law 95-507 without doing violent, destructive kinds of things to those people with whom you have dealt over a period of years.

Again, I just want to commend you. My own feeling is if the heart and the mind are right, then the rest of the body will move along in the right direction.

It appears to me that you are moving in the right direction. The allegations that you heard earlier today from one of the witnesses, I have asked him to substantiate those allegations and give me more facts. Once they are received, I would like to be back in contact with you.

Mr. KLINE. I hope you would. We understand the situation.

Mr. MITCHELL. I certainly would not want your company to have its reputation tarnished by some untoward act, if indeed the allegations are correct.

Congressman Hatcher?

Mr. Hatcher. Thank you, Mr. Chairman.

I would just like to say, it concerns me and seems to be somewhat inconsistent that Public Law 95-507 causes a company like yours to be perhaps overburdened in reporting requirements and yet all the testimony we have heard prior to you today is that those companies that do not comply and perhaps do not have the social conscience that you do or willingness to comply with the Government's requirements are not being punished.

The chairman says he is concerned about that, too. I have heard him make that statement. Certainly that is something we want to look into. If it is a burden for you, we should find a way to lessen that burden and certainly should make all companies comply with the requirements.

Mr. KLINE. That is the area I wanted to address a moment ago. I just want to say, this area of compliance and the monitoring for compliance—I am somewhat disturbed at the inference that there are companies that don't comply. I am wondering what magic they found, because it is not just a question of whether we want to or don't want to. You must, or you don't stay in our kind of business.

You are reviewed for compliance. There are people on Mr. Trimboli's staff, there are people in the local DCAS—Defense Contract Administration Services—office, who are in our plant almost monthly, reviewing our records and auditing them to insure compliance, to insure that when I give you numbers like we did today, that those are accurate numbers.

Now, are they only visiting me? Who is visiting these guys that are breaking the law?

Mr. MITCHELL. I think the response can be couched in these general terms. I refer to the genius of the private sector in almost creating miracles. There are portions of the private sector that also have a genius for not being in full compliance with certain regulations.

Now, I will be the first to admit that some are finding ways not to be in compliance. In our hearing in Los Angeles or Chicago, there were 42 companies that had been cited by the SBA.

A part of the problem is with the Agency itself. DOD should never sign off on a contract that is not in full compliance. Part of the responsibility is with SBA. Part of the responsibility on the failure to live up to responsibility on the part of both agencies is reflected in the lack of personnel to do the adequate followthrough. But somehow or another we are going to see that the law is obeyed. I am glad that you are a partner in that kind of cooperative venture.

Thank you.

Mr. KLINE. Thank you.

PANEL CONSISTING OF: BRENDA SMITH AND ROBERT I. BRICKMAN

Mr. MITCHELL. Our next panel is Ms. Brenda Smith, Deputy Director, Governor's Office of Small Business, and Mr. Brickman. It is good to see you again.

TESTIMONY OF BRENDA SMITH, DEPUTY DIRECTOR, GOVERNOR'S OFFICE OF SMALL BUSINESS DEVELOPMENT

Ms. SMITH. My name is Brenda Smith, and I currently hold the position of deputy director of the Governor's office of small business development.

Gov. Bruce Babbit and my office wish to thank Congressman Parren Mitchell and the committee for holding today's public hearing in Arizona, as well as welcome you to the State.

The testimony that I am offering the House Small Business Committee today will begin with a short overview of legislation introduced during the 1981 State legislative session.

The recently completed legislative session was a fruitful one for small businesses in the State of Arizona. A large variety of bills were introduced during the session that would, if passed, have affected the Arizona business community. Of these bills, the following six passed both houses and were signed into law by Governor Babbit. They are currently law.

Senate bill 1005, the shared work unemployment compensation program.

This bill seeks to reduce worker layoffs during economic recessions by instituting a shared work unemployment compensation program. This voluntary plan, created by the employer, allows employers to reduce workers' hours rather than lay off workers.

Shared work benefits, essentially a form of unemployment insurance, allow employers to keep rather than layoff their workers.

A shared work plan can be developed for as few as two workers. Any employer can participate in this program providing unemployment benefit contributions are up to date and assurances of proper management are given to the State of Arizona. The shared work benefit would be computed from the difference of the regular number of hours worked and the reduced number of hours.

As stated in Senate bill 1005, parts of the shared work plan will become effective on December 31, 1981, and other provisions will take effect on December 31, 1983. The shared work unemployment compensation program will allow employers to retain their workers even in times of recession. Consequently, this bill offers methods to keep down unemployment in Arizona, and provides a means whereby both employers and their workers can weather bad economic times.

SENATE BILL 1009—THE TAX CUT BILL

Senate bill 1009 reduces taxes by increasing State aid to education an estimated $15.5 million, increasing the State's share of homeowner school taxes to 53 percent from 45 percent, reducing school district qualifying tax rates a dime and setting the State property tax rate, which is currently $1.25, at 95 cents. Arizona businessmen will partake in the benefits of this property tax reduction.

SENATE BILL 1010—DEPARTMENT OF REVENUE: COORDINATION OF BUSINESS LICENSING

This legislation provides the mechanism, whereby, a person desiring to engage in business may obtain certain tax identification numbers and licenses from the Department of Revenue.

By filing a single form, a person desiring to begin a business may obtain employment identification numbers for income tax withholding and unemployment insurance purposes and transaction privilege tax licenses, and any other identification numbers and licenses deemed practical.

Businessmen should find this one-stop shopping approach to business licensing both practical and positive. It should substantially facilitate the starting or conducting of a business in Arizona.

Previous to this bill, there were four or five different steps a businessman had to take prior to opening a small business.

SENATE BILL 1033, HAZARDOUS WASTE DISPOSAL SITE

The passage of this bill provides for the acquisition of a hazardous waste disposal site by the Department of Health Services. Also established by this bill is a buffer zone and an easement for access to the disposal site.

The enactment of this legislation will greatly influence many Arizona businesses. An instate disposal facility assures industries with hazardous waste byproducts that their wastes will be handled in an environmentally sound and economical manner.

SENATE BILL 2017, VOCATIONAL EDUCATION COST STUDY

This legislation provides a supplemental appropriation to the legislative council for the funding and reimbursing of costs associated with the contracting of: One, a vocational education cost study; and two, a transportation cost study.

Of most interest to the business community would be the vocational education cost study. This study will pave the way for increased attention to vocational and technical training throughout the State.

HOUSE BILL 2229, EQUAL ACCESS TO JUSTICE

The purpose of this bill is to provide for the award of fees and other expenses to a prevailing party—other than the State of Arizona—in certain civil actions in which the State is a party.

This legislation benefits individuals, partnerships, corporations, and other organizations by: One, reducing the economic deterrents involved in contesting governmental action; and two, entitling prevailing parties to recover an award of reasonable attorney fees, expert witness fees, and other costs against the State.

This bill, which was voted the top legislative priority at the recent State Small Business Conference, will have the effect of restraining unreasonable and unjustified State government regulations.

Unfortunately, there was additional legislation before the State legislature which would have been of benefit to small businesses and did not reach the Governor's desk. Perhaps the most important was Senate bill 1377, a bill which the Governor called for in his state of the State address. That would have established a State investment tax credit. As proposed, it would have provided for $10 million in business tax relief.

At the State small business conference, many participants expressed support for the concept of improved oversight of agency rules and regulations.

I agree that rules and regulations should avoid unnecessary duplication and that needlessly costly and excessive rules and regulations are not in the public interest.

To this end, Governor Babbit has established the Governor's regulatory review council. This council, which is composed of five members, will review all agency rules and regulations which have an economic impact on all State government or its political subdivisions.

The council will determine if the benefits outweigh the cost imposed, the draft rule or regulation is clearly and understandably written, and the public interest is served.

If the council finds the proposed cuts or regulations do not meet the cost/benefit, above-mentioned standards, it will be returned to the agency for revision and reconsideration. It is my hope that this process will guarantee a comprehensive review of the impact and effectiveness of State agencies' rules and regulations.

The remainder of my testimony is designed to give you a better understanding of what the office of Governor Babbitt is doing in support of the small business community.

Shortly after the State small business conference, Governor Babbitt established the Governor's office of small business. He then appointed Bernard David, director, and myself as the deputy director, so that we might be able to actively aid and assist small businesses with any problems they may have while doing business with State agencies. This office, which officially opened on July 1, 1981, is the first of its kind in Arizona.

During earlier testimony you had a question, asking if there was a State minority business set up. You may have referred to the Governor's office of small business. It is the Governor's office of small business.

Currently we do not have a minority business office. We also do not have an affirmative action plan for our State purchasing department.

Mr. Mitchell. You don't?

Ms. Smith. We do not. In my investigation, we also do not have State set-asides in our purchasing department. We do have an affirmative action plan at the Arizona Department of Transportation, though. But I believe that is because they are under a Federal mandate because they get an awful lot of Federal moneys there.

But in the general State purchasing department and the State university, they do their own purchasing. I don't believe that—and I am still doing research on that—there are any such plans in the State. I think that there is an executive order around saying that there should be fair treatment to minorities as well as everyone else.

But I am not sure. I know there has been legislation introduced in the past for set-asides for small and minority businessmen. But it is my belief none of those bills have passed our State legislature.

As well as being an ombudsman or advocate for small businesses, the Governor's office of small business will also be responsible for looking very closely at Federal, State and local programs, as well as legislation that affect the small business community.

Some of the programs that we will research are SBA's new 503 development company program, the economic development administration development finance program, SBA's 502 development company program, Farmers Home Administration business and industrial loan program, and SBA's 8(a) program.

Realizing that the present mode of Congress, which is to reduce Federal spending, means that some economic development programs may be reorganized or cut out of existence, one program that should be well funded is the Small Business Administration.

Our Federal, State, and local governments are completely dependent on the tax base created by the private sector. Without this real wealth, there would be no money for education, social services, national defense, law enforcers, or any other governmental tasks that Government undertakes.

In Arizona we are in a transition period in our State's economy from agriculture mining service to one which is heavily oriented toward manufacturing. This is an extremely important change since it dramatically influences our tax base which directly or indirectly provides the revenue to rebuild and reorient our total system of education, construct, reconstruct, and maintain our network of streets and highways, and provide the resources necessary to block the wave of crime which is spreading across our State and Nation.

Therefore, since it is a clear fact that the private sector plays an important role in the Nation's economy, it seems as though the Government should be in the business of aiding our businesses.

Let it be known that the Governor's Office of Small Business, the executive office of the State of Arizona do fully endorse and support SBA's programs.

I would like to end by thanking Congressman Parren Mitchell and the U.S. House of Representatives Committee on Small Business for allowing me to express my views, as brief and general as they were, to this field hearing held today in Arizona. It has given our newly established office vital information from the testimony that I have listened to today, so we can now be in a better position to develop the kind of agency that will be responsive to the small and minority businesses in Arizona.

Our office also wishes to thank all of the business people who attended and spoke today, and Tom Trimboli for the help his office has given us since we have been in existence.

Thank you.

Mr. MITCHELL. I guess I am a little troubled. Ms. Smith, you are relatively new on the job. And I guess I was sort of stunned by the absence of any affirmative action within the State government. I would hope that you would be in the vanguard to try to correct that deficiency.

I would further assume that since you are so new on the job, it would be virtually impossible for you to give this committee any information about minority business participation in any of the State building that is going on, the State roads repair, in any State activity. Would you have any such information available?

Ms. SMITH. We have no affirmative action policy with regard to small business, but we do have a State affirmative action office in employment.

Mr. MITCHELL. I said affirmative action program for minority business. It just seems to me that the State places itself in a very awkward position when it exhorts the private sector, such as Motorola to do well, and pleads with it to do well on behalf of minorities, yet at the same time it has this gross deficiency.

More specifically, my question is: Would you today have any data at all on minority business participation in any State activity that would include the State universities which do their own procurement? Would you have any data on that at all?

Ms. Smith. No; we might have some information on the department of transportation. They have a different affirmative action program. That is a State agency.

Mr. Mitchell. As you move in this new position, would you plan to do that sort of thing?

Ms. Smith. I am planning on gathering that type of data. Presently all that our office has been able to do is get new furniture and get phones in. I have spoken with the State purchasing department. I had a complaint from a minority businessman. He said he had been attempting to do business with the State for 11 years, and he is always the next to the last bidder.

When I went over to State purchasing, that is when the problem was raised that at one time—he couldn't remember when—there had been a set-aside program for minority businessmen, but there were not enough minority businessmen, he said, in order to actively participate in the program. Therefore, the State dropped the program. And it was not statute.

Mr. Mitchell. I am not referring to set-aside, which is infinitely preferable to me. I believe in set-asides for minority businesses. I am talking about taking the first basic step of establishing an affirmative action for minority business participation in State activities which cannot be equated with set-aside.

Congressman Hatcher.

Mr. Hatcher. No questions.

Mr. Mitchell. Thank you very much.

Mr. Brickman, I understand you want to speak to the antitrust laws in Arizona.

TESTIMONY OF ROBERT I. BRICKMAN, ARIZONA ATTORNEY GENERAL'S OFFICE ON ANTITRUST

Mr. Brickman. Yes; I do.

As the attorney general referred to it last night, antitrust has been regarded as a "dirty word," because few people understand its meaning. This is a serious problem.

What I would like to do is briefly highlight what we do in the antitrust division, and our fundamental role in working with the small business community to preserve their status as competitors in the marketplace.

Antitrust basically refers to competition. Anybody schooled in antitrust law should be considered a competition expert. Let me illustrate the types of things that we deal with, especially from small business perspective.

A small businessman complains that his suppliers have agreed to discontinue the granting of any credit on his purchases, for example going from 30 days' credit to cash in advance or cash on receipt. This may be a form of price fixing, which is illegal.

Or, small businessman complains that his competitors, all major prime contractors, have told him that he cannot bid on a particular contract. If he does, they will drive him out of business. But if he refrains from bidding, they will make sure he gets a small contract sometime in the future. This may be a bid rigging conspiracy, monopolization, price fixing, all of which might be illegal.

A small businesswoman opens up a boutique, offers to sell designer jeans, designer perfumes, and other such items. She advertises a price below that of her competitors, the large retail department stores. She is told by her supplier if she continues to advertise by herself she will be terminated. She is further told that if she sells her products at less than an established price, she will be terminated. These examples illustrate resale price maintenance, which may be unlawful and illegal.

Suppose a small business who carries a number of business machines or computers has a request from many of its customers to carry a new machine. He contacts the manufacturer, the manufacturer says, "Fine, I will send you as many as you need. However, in order to sell this machine you must also carry all my other products." The small business cannot afford to do that and his customers have no interest in the other products. What does he do? This is an illustration of a tying arrangement, which maybe illegal.

A small businessman is looking to handle some construction work, but cannot find bonding; or, he is looking to expand or start a business, and he goes to several banks. Let's assume the business is credit worthy, a good risk, and he should qualify. But no one will give him bonding, and all the banks will charge the exact same percentage rate above prime, and the same repayment schedule. Is this prudent business conduct or do we have an illustration of unlawful refusals to deal?

When these types of complaints are brought to the attention of the appropriate antitrust authorities we can make inquiry, and determine whether we can assist the small business in being able to compete fairly and effectively in the marketplace.

What if a small business calls your office and complains about a proposed regulation by a governmental agency which will implement a legislative program in such a way that it discriminates against minority small business, or it imposes requirements not set forth in the statute, or the proposed regulation fails to carry out the express provisions of the statute. What do you do? What advice do you give him?

The competition experts, people skilled in antitrust, may be able to help. At the Federal and State level, the antitrust divisions represent regulatory agencies: It is our job to make sure that their conduct does not violate the laws of competition and fair practice, and merely because it is a government agency acting does not mean that the conduct is proper or legal; it is our job to make sure that government officials don't exceed their statutory authority or intentionally refuse to carry out their statutory authority in such a way that it discriminates against small business; and it is our job to make sure that all rulemaking, rules, and regulations passed by agencies foster competition, not inhibit and restrain competition.

In addition, the antitrust divisions at both the State and Federal level advocate competition. We work with legislators to make sure that proposed laws foster competition, and we do our best to make sure that laws that will inhibit competition, or that will enable certain companies to monopolize an industry, are absolutely necessary to protect a legitimate public interest.

Finally, we work with the business community. The antitrust division in the State of Arizona is always available to speak and meet with any trade association, any groups of businesses to discuss the "nuts and bolts" of fair competition policy.

Sometimes a little familiarity with the antitrust laws by small businesses will prevent a small business from being later found guilty of violating the antitrust laws. It might also alert him that there is an anticompetitive practice going on which he can report to us and which we may be able to eliminate.

Our most difficult job is detecting and attacking institutionalized anticompetitive practices. We are talking about an industry that may have been born in an environment of competition, but like a tree each year a new layer of regulations or barriers are added. Eventually you have what was once a competitive industry now controlled by four or five companies. It might be outrageously expensive for a small business, especially a minority business, to raise the capital to enter the industry and the rules of the marketplace have become so ingrained that people accept them as the way of doing business, thereby making it difficult, if not impossible, for a small business to compete.

Oftentimes we cannot detect these institutionalized practices because they are so complex. It is like a maze. If we don't have small businesses who recognize the practices, come forward, and make disclosure and assist us, there is no way we can eliminate anticompetitive institutionalized practices.

Our job is to get at the roots of these institutionalized practices. Only then can we restore the competitive balance to the marketplace. In order for there to be competition, we need small businesses. Without small businesses there is no safeguard for competition.

Institutionalized practices sometimes grow out of legislation. As the Congressman is well aware, when the Maybank amendment was first enacted, there may have been good cause for it. But after 26 years, that cause was no longer obvious, apparent or necessary, and it took a lot of energy to finally rid the small business community of the unfair practice embodied in that amendment.

We also may find institutionalized practices created by regulatory fiat. The present procurement practices at the Federal and State level facilitate the sole sourcing of contracts and the common practice of "wiring" a contract to a specific company.

Again, once a practice is detected and brought to the attention of the appropriate antitrust or competition expert, we can either pursue a vehicle of lawsuits, work with the appropriate regulatory boards and agencies to change the regulations, or work with the legislature to change the laws.

These are a few recommendations for improving Federal programs to assist small business:

First a message must be carried to the small and minority business community that antitrust is synonymous with competition. Just as small business represents the backbone of our economy, antitrust, or the competition laws, represents the guardian of preservation for small business; we should be viewed as a partnership, but through the connotation of the word antitrust, antisomething, we have never been further apart. We recommend Federal assistance to carry the message to the small business community to become familiar with the antitrust laws.

When I worked for the Antitrust Division of the U.S. Department of Justice in Washington, the easiest cases to prosecute were price-fixing cases against small businesses. Why? Because they were usually unsophisticated in business or competitive practices, they could not afford experienced antitrust counsel, and often they would document or record their agreements to fix prices. They are what we refer to as "smoking gun" cases. A small business today convicted of violating the Federal antitrust laws faces a fine of up to $1 million and mandatory imprisonment; the fines are not as severe at the State level.

It is indeed ironic that neither the Department of Justice nor the Small Business Administration does anything to assist small businesses in learning about competition. We give small businesses management and technical assistance, loan assistance, and procurement assistance. But once they are out in the competitive jungle, we desert them.

Finally, we recommend that the Federal Government look carefully at legislation, especially disguised legislation, which may be detrimental to the small business community. Also, be aware of good legislation that is mischaracterized as bad legislation. Two examples:

First, a bill that has been introduced, S. 995 and H.R. 1242, which would authorize contribution among defendants in price fixing cases. Another name for this legislation, and the more appropriate name in our estimation, is the "Price Fixers Relief Act of 1981." We urge the committee to review the testimony that was submitted to Chairman Rodino of the Judiciary Committee and to take an appropriate stance.

Second, an illustration of a good piece of legislation that has been characterized as bad, *Illinois Brick* legislation. A 1977 Supreme Court decision ruled that only a direct purchaser from a manufacturer of a price-fixed good could sue to get damages. Very few small businesses purchase directly from the prime manufacturer. Therefore, there is a detrimental and disproportionate effect on small businesses who may be forced to pay higher prices for a price-fixed product, but cannot sue to recover his damages because he is an indirect purchaser. Legislation which would overrule the Supreme Court has been defeated during the last two Congresses.

Again, I thank you for this opportunity to share with the committee the views of the antitrust division of the attorney general's office on antitrust and its important role for the small business community.

[Mr. Brickman's prepared statement on behalf of the Arizona Attorney General's Office follows:]

Prepared Statement of Robert I. Brickman, on Behalf of the Arizona Attorney General's Office

INTRODUCTION

Mr. Chairman and Members of the Small Business Committee. I am pleased to appear before you on behalf of the Arizona Attorney General to provide you with suggestions for improving Federal programs designed to help small and disadvantaged businesses overcome impediments to their continued development.

The relationship between small business and the enforcement of the antitrust laws is perhaps one of the best kept secrets in the small business community. However, the future of small business in Airzona, and elsewhere, will depend in large measure on vigorous and effective enforcement of state and federal antitrust laws. The fundamental purpose behind the antitrust laws is to foster and promote the process of competition and free enterprise. In so doing, we preserve the right of every person to engage in any lawful profession, trade or occupation of his choice;

and we preserve the right of small businesses to grow and prosper to the fullest extent of their potential unrestrained by the anticompetitive actions of others.

My testimony will briefly review the role of the Antitrust Division of the Arizona Attorney General's Office, the relationship between small business and antitrust, the partnership between Federal and State antitrust enforcement in making competition work, and finally, my testimony will offer several suggestions for improving federal programs designed to aid small business.

STATE ANTITRUST DIVISION

The Antitrust Division of the Attorney General's Office is responsible for the implementation of the office's policies for the enforcement of the antitrust laws and the promotion of competition and deregulation. The Antitrust Division investigates and prosecutes federal and state antitrust damage actions on behalf of the State of Arizona, its political subdivisions and consumers within the State as well as investigating and prosecuting actions under state antitrust law. In addition, the Antitrust Division counsels other state agencies on matters relating to antitrust and competition and has presented testimony before the Arizona legislature and the United States Congress on these matters.

The Antitrust Division began as a section of the Economic Protection Division in 1975 and effective October 1, 1978, was elevated to its present status as a full-fledged division. Its growth has been aided by federal grants under section 116 of the Crime Control Act of 1976, Pub. L. 94-503, 42 U.S.C. § 3739 and by the Antitrust Enforcement Revolving Fund, Ariz. Rev. Stat. Ann. §§ 41-191.01 and 191.02, through recoveries from antitrust litigation. The Antitrust Division is presently staffed by six attorneys supported by para-professional and clerical staff. The Antitrust Division has proven to be very cost-effective. During the years of its operation, more than five dollars was returned to the State, political subdivisions and taxpayers for every dollar spent for antitrust enforcement.

In the area of deregulation, the Attorney General's Office has embarked on a comprehensive review of the State's regulation and licensing of occupations and professions and its impact on the small business community. Our goal is to eliminate the anticompetitive aspects of state regulation, and provide the business community with a simplified scheme of regulation which will protect the public health, safety and welfare, and create a business climate which is favorable to fostering competition. We will be submitting proposed legislation for the next legislative session.

Future enforcement activity of the Antitrust Division will concentrate on consumer goods and services. In addition, the Antitrust Division will continue to be active in encouraging and promoting deregulation.

RELATIONSHIP BETWEEN SMALL BUSINESS AND ANTITRUST

The policy of the Congress to "aid, counsel, assist, and protect . . . the interests of small-business concerns" is premised on the recognition by the Congress that—

The essence of the American economic system of private enterprise is free competition. Only through full and free competition can free markets, free entry into business, and opportunities for the expression and growth of personal initiative and individual judgment be assured. The preservation and expansion of such competition is basic not only to the economic well-being but to the security of this Nation. Such security and well-being cannot be realized unless the actual and potential capacity of small business is encouraged and developed. (Sec. 2(a) of the Small Business Act).

The important role of small business to our nation's economy often is overlooked or misconceived. For example, small business is the single biggest creator of new jobs; the small business community is directly responsible for most of the research and development which leads to greater productivity; small businesses historically have been "hotbeds" of entrepreneurship and innovation, accounting for over half of major innovations; and small business accounts for more than 50 percent of all private employment and 43 percent of the gross national product.

The antitrust laws evolved because of Congressional concern that certain types of conduct by powerful business organizations threatened to undermine the ability of small businesses to effectively compete, and thereby threatened to undermine the American economic system of private enterprise.

Let me describe the general types of conduct which have been condemned by the Congress and the Courts as violating the antitrust laws: agreements to restrain trade, price fixing among competitors, agreements to divide markets or customers, agreements to limit production or to limit expansion of services, agreements to boycott, price fixing between manufacturers or other suppliers and those below them in the distribution chain, (e.g., retailers,) tying arrangements, bid rigging and monopolization.

The Small Business Act makes specific reference to the role of antitrust in *safeguarding small business in Section 10(c)*, which directs the Attorney General to submit yearly reports to the Congress setting forth the results of "surveys of any activity of the Government which may affect small business, for the purpose of determining any factors which may tend to eliminate competition, create or strengthen monopolies, promote undue concentration of economic power, or otherwise injure small business" and setting forth appropriate recommendations.

To illustrate the perceived importance of antitrust enforcement by the small business community, of the sixty recommendations made by the delegates to the January 1980 White House Conference on Small Business, antitrust ranked fortieth:

The merger and acquisition antitrust laws should be amended to: (1) inhibit monopoly and conglomerate growth of giant companies, provided safeguards are built in to protect the small business, (2) prohibit dual distribution that adversely affects wholesalers, distributors, dealers, retailers, and franchisees; and (3) prevent the termination or non-renewal of wholesalers, distributors, dealers, retailers and franchisees without good legal cause.

ROLE OF SMALL BUSINESS IN ANTITRUST

Given the role of antitrust to preserve and protect the competitive market place, and thereby facilitate the entry and operation of small businesses in the market place, what then is the role of small business in antitrust? The small business community basically has two roles to fulfill: Its first role is to avoid engaging in anticompetitive practices. Its second role is to detect the anticompetitive practices of others. Both roles require the small business to have some familiarity with the antitrust laws. I will address the problem of how the small business obtains that familiarity later in my testimony.

The second role, detection of anticompetitive practices, is crucial for effective enforcement of the antitrust laws. Small businesses are in the best possible position to detect anticompetitive practices in the market place, because they are generally affected by those practices, directly or indirectly. For example, an agreement by competitors not to do business with the sole manufacturer of a product unless he terminates a small business distributor who has been engaging in discount pricing, may effectively foreclose that small business from receiving that product; and practices by a small business' competitor to monopolize the market may drive that small business out of business.

Once anticompetitive conduct is detected, a small business has three options: (1) Pursue his own antitrust action to stop the conduct and collect provable damages to his business; (2) report the conduct to the appropriate state or federal antitrust authority and agree to cooperate in any subsequent investigation and trial; or (3) do nothing.

The first option is sometimes too costly for the small business to undertake, and by exercising the option of doing nothing, the small business allows the competitive market place, and perhaps his own business, to suffer. The second option, therefore, is the most promising for the small business. In this instance, the State or Federal authority will have greater resources available to eliminate any illegal practices.

RELATIONSHIP BETWEEN STATE AND FEDERAL ANTITRUST ENFORCEMENT

Although Federal antitrust enforcement has been around since the 1980's state antitrust enforcement is a relatively recent phenomenon. Most state enforcement programs came about as a result of the Grant Program to Aid State Antitrust Enforcement, authorized by Congress in Section 309 of the Crime Control Act of 1976. This program provided a three-year "seed" program of assistance and grants to states to improve their antitrust enforcement capabilities. One of the sponsors of the bill, Senator Morgan of North Carolina, emphasized the role of the states in assisting the small businessman stating "It [the bill] encourages states, through their Attorneys General to make sure that the small businessmen's livelihood, and the consumers hard-earned money are not taken from them by illegal acts." Recognizing the inadequacy of staffing for antitrust enforcement in those states with antitrust laws, Senator Morgan stated:

This [bill] will improve that situation, and it will do so in a manner agreeable to all those of us who believe strongly in the principles of states' rights. *The States are ideally situated to protect the rights of* the consumer, *the small businessman,* and the honest businessman of any size. By means of this [bill], we will give the States the funds to make a beginning. (Emphasis supplied.)

Congress has also provided the states with additional enforcement tools. For example, the Hart-Scott-Rodino Antitrust Improvements Act of 1976 gave the states the power to bring parens patriae suits under the federal antitrust laws, which enables the states to bring damage suits on behalf of consumers.

Cooperation between the Federal and State agencies has resulted in coordination of investigatory efforts to eliminate duplication, in the referral of complaints and other relevant information, and has resulted in a partnership in making competition work.

While the road to this "partnership" has been a little bumpy, the Federal government recognizes the states' vital role in bringing the benefits of competition to their citizens, and the fact that most businesses are still local and non-national in scope. Thus, there are sufficient numbers of possible antitrust violations to keep both state and federal authorities busy.

RECOMMENDATIONS FOR IMPROVING FEDERAL SMALL BUSINESS PROGRAMS

I would like to make the following recommendations, or suggestions, for improving Federal programs designed to help small business overcome impediments to their continued development:

1. The Department of Justice and the Federal Trade Commission should continue to cooperate with the states in antitrust enforcement.
2. The federal government should increase its role in familiarizing small businesses with federal and state antitrust laws. While I am aware of a pilot program by the Federal Trade Commission to provide small businesses with the basics of competition and trade laws, I am aware of no undertakings by either the Department of Justice or the Small Business Administration. This is indeed ironic because of the important role which small business can play in antitrust enforcement.
3. The Congress should continue Federal assistance and grants to states to improve and maintain their antitrust enforcement capabilities and to develop outreach efforts to familiarize small business with antitrust laws and policies.
4. The Small Business Committee should oppose legislation authorizing contribution among defendants in antitrust cases. We believe that S. 995 and H.R. 1242 "will unnecessarily complicate antitrust damage litigation, will confuse and hinder the settlement process, and will diminish the deterrent effect of the potential treble damage claim."
5. The Congress should consider legislation to give "indirect" purchasers of price-fixed goods the right to sue under the antitrust laws to obtain treble damages. A 1977 Supreme Court decision, *State of Illinois* v. *Illinois Brick Co.*, limited antitrust claims to direct purchases, thereby preventing in most cases recovery by all other purchasers who are further down in the chain of distribution. That decision has a disproportionate effect on small businesses since many do not purchase directly from manufacturers or large distributors.
6. The Small Business Committee, and other appropriate Congressional Committees, should review the impact of federal antitrust policy and federal regulations on the ability of small businesses to enter and compete in the market place of their choice, similar to what the State is doing.

Mr. Chairman, thank you again for providing the Attorney General's Office with the opportunity to testify.

Mr. MITCHELL. Thank you.

I have one last witness. It is my fault I overlooked this witness. Mr. Simpson of the Southwest Area Minority Contractors Association.

If you will be seated and make your statement, we will be glad to hear from you. Thank you for being patient.

While I am at it, why don't I thank the entire audience for being here all day with us. I know I have learned a significant amount of information. One of the problems with having these field hearings is that after the hearing you end up with 3 months' work for the staff to follow through on. But I do thank you for all your participation today, and for a wealth of information that we will definitely follow through on.

Mr. Simpson, please proceed.

TESTIMONY OF MIKE O. SIMPSON, PRESIDENT, SOUTHWEST AREA MINORITY CONTRACTORS ASSOCIATION, PHOENIX, ARIZ.

Mr. SIMPSON. Mr. Chairman and members of the committee, I am Mike Simpson of the Southwest Minority Contractors Association. We are pleased that you found time to squeeze us into this hearing, to give testimony in regard to contracting, construction business in the State.

As you well know, Mr. Chairman, as you travel this Nation far and wide, and you know all of the problems that are confronted by minority contractors.

Now, we here in Arizona are no different. We have some of the same problems that other businessmen have across this Nation. And that is in regard to capital, bonding, the whole spectrum that construction contractors go through. One of the problems that we have here in the State is Federal contract compliance.

First of all, you just heard testimony that the State of Arizona does not have an affirmative action program. We have a lot of problems in this State with regard to Federal contract compliance, that is, the various Federal agencies who do have affirmative action offices and people to oversee compliance are just flat not doing their job.

I heard Mr. Trimboli say this morning that the various agencies and compliance offices don't have enough teeth to do any enforcement. I had the privilege to be involved with some of the city of Phoenix personnel in regards to affirmative action and compliance and what have you. This young man was doing such a tremendous job—this was one of the only times I ever saw where he called people in on a compliance review and also made them come up with a show cause why they were not in compliance.

And there has been one job in the city of Phoenix, construction work, that was shut down and the contractor's money was stopped because he was not in compliance. Now, this young man, he happened to be black, the affirmative action officer for the city of Phoenix. He made too many waves for the establishment, and he was conveniently given a promotion. Ever since then, there hasn't been too much compliance in any area, Federal, State or local.

Now, some of the problems we have been having outside of compliance are we have a lot of minority fronts here who are certified by the State. The State department of transportation has a MBA program. And in this program they go out and certify potential minority businessmen and contractors to do work on State projects. They send out some of their personnel and also they did have a consulting firm come out and look you over, you might say. They have forms you fill out to verify whether you are minority or whether you are the owner of this company, 51 percent or more. And they look at some of your financial records, see who signed the checks, and who is really responsible for this company.

Half of the people on the list are minority fronts. We had some fellows in here this morning with regard to the 8(a) program. Some of your largest and most well-off minority contracting firms in this State are not on the 8(a) program and don't need to be on it, and they are not trying to get on it. I would say the top 10 has never been on it and have no use for it.

Half of those are minority fronts. We, as an organization, are aware of this. And also the various agencies are aware of it. But the word is how can they prove it. No one has filed any type of a legal matter in regard to trying to eliminate these people, and the State Department of Transportation is not going to. They feel that these minority fronts are the minority that is keeping them in compliance on these construction jobs.

Mr. MITCHELL. Let me interrupt you just a minute at that point. I have consistently heard the charge about minority fronts, and there is nothing that would anger me more than a minority front company. We have, under present law, criminal provisions for dealing with minority front companies. Indeed, any misrepresentation to the Government in most instances can be deemed an offense against the Government, punishable by fine, imprisonment, or both.

What has distressed me as I have traveled around the country is that I hear statements such as yours, and rarely does anyone give me the name of a firm and some background to show that indeed this is a minority front company. That is all that I want. I would not ask you to do that at this hearing. But if you have some conclusive evidence to show that these are front companies, please get it to me. I am now dealing with one in Washington. We are investigating it there. I have enough information to suggest that it was a front company. Therefore, we could move through our investigative committee. But it is awfully difficult to give me that general statement and not to give me a name and facts to substantiate the allegation that is being made. I hope that you will, because I think these operations are an abomination.

Mr. SIMPSON. Mr. Chairman, we will send you a listing of every minority front in this State.

Mr. MITCHELL. And the justification for your allegation that it is a minority front. I need that.

Mr. SIMPSON. All right.

The second thing I have to say here is in regard to some of our major corporations, which we had the Motorola firm here a few minutes ago. The Motorola firm is such a large division—I understand they are the largest employer in the State. The Motorola firm, along with several others, have a policy in regard to minority procurement and use of MBA's—a lot of their job is not put out in open bid. Most of their job is negotiated contracts with the same outfits.

I heard Mr. Hatcher speak this morning in regards to belonging to the country club, being one of the boys in the backroom, and that type of thing. That is the way it is with many of these major prime contractors that have Government contracts. You cannot break into the system. They have a thing they call a select list of bidders. If you are not one on the select list, you are not going to ever get any work with them.

Their record—not only Motorola, but some of the large outfits in this State, the compliance office is fully aware of—have been told verbally and in writing, and they have no enforcement power whatsoever. They don't know who to turn to. And some of those outfits are the Motorola Co., Honeywell, Sperry, and Mountain Bells. If you look at their record and see who has done construction jobs for them over the past 2 to 3 years, you see the same people doing it all the time. There is no competitive bidding. I am sure that you can have access, to get those records to see exactly what is happening in those areas.

Furthermore, the SBA 8(a) program is lacking in a lot of areas. First of all—I want to say this here. We only have 25 slots for applicants for the 8(a) program. Out of those 25, 24 are active. There has been one vacant slot for quite some time. Out of those 24, there are 8 of these contractors that are minority contracting firms. Six of those are Mexican American, one black, and one Indian. Now, it is really a shame that the largest 8(a) contractor in this State happens to be a janitorial firm—when you have eight contracting firms on the 8(a) program.

Now, since Mr. Trimboli has been Director here, as you heard his figures this morning, the 8(a) program has really taken off, and they are doing much better than what it used to be, a great deal better as far as getting procurement and money toward construction projects for these 8(a) contractors. Before that, they were just giving them crumbs and handouts, difficult jobs that nobody wanted to do. So they just gave that to an 8(a) contractor. Now it is getting much better. I have to say that while Mr. Trimboli is here listening, and he also has the same staff down there, it seems to me that he is applying the whip in the right places and we are getting better results.

Finally, we have a serious problem here in the State, and it is in regard to some of our HUD 8(a) section 202 contracts that have been let in this State. One in particular really—the Minority Contractors Association—we have a serious problem with HUD, and HUD's contract compliance. First of all, we just had recently a contract let—as a matter of fact, it is still under construction, the section 202 that I am speaking of here.

There was complete and total disregard for the minority contractor. The building itself was in excess of $4 million, the total contract was $6 million. This was the latest section 8, 202 project that was let in the State of Arizona by HUD. We had a problem with that.

Our association met with the owners and met with the general contractor, the prime contractor. We had heard so many rumors. There has been such a lack of information and information has been withheld. This particular incident is really a shame and a sin, that something like this could happen.

I don't know all of HUD's regulations in regard to compliance and in regard to affirmative action on the 8(a) section 202 projects. But the Phoenix Urban League was given this contract, section 202, and the building is still under construction. That was one minority firm on that project, $6 million, at a tune of $32,000 was the amount of his contract—one minority firm. And when we confronted the HUD regional office over in California in regard to this, HUD said, their response to that was that the Phoenix Urban League was the contractor and they were the minority firm and therefore they did not have to hire minorities to construct this building.

Now, we had five members of our association bid at various phases of the work. We bid at the job. Two of the contractors were the lowest bidders. They still were not awarded the contract. The prime contractor who received the bid, received the bid not in competitive bidding. He was awarded a contract through negotiations. He selected, which he already had, his own subcontractor and performed the job. The minority contractor was left out of the project completely.

Mr. MITCHELL. This is certainly one we want to take a look at. No matter what the regulations are, HUD is still covered under Public Law 95-507 and ought to be in compliance.

Mr. Simpson, ladies and gentlemen, I have been warned we will get locked into this building within 5 minutes. I have no intention of spending the night in this hearing room. Therefore, I regret that I am going to have to cut you off so we can get out of here. I assume you don't want to be locked in either. I would appreciate it if you would get someone to type up your testimony, the balance of it that we have not covered. What you covered up to this point is OK, and get it to me. I am sorry; I was unaware of the fact that we have to be out at 5 o'clock. I just learned about it.

Mr. SIMPSON. In closing, Mr. Chairman, I am hoping that your time wasn't wasted and my time wasn't wasted. I am hoping that the small business hearing will not be as a lot of the other Federal bureaucracy.

Mr. MITCHELL. That is certainly not my intention, to waste my time here. I have come to do work. Thank you very much.

[Whereupon, at 4:55 p.m., the committee adjourned, to reconvene subject to call of the Chair.]

SMALL AND MINORITY BUSINESS IN THE DECADE OF THE 80's (PART 2)

MONDAY, JANUARY 18, 1982

House of Representatives,
Committee on Small Business,
Atlanta, Ga.

The committee met, pursuant to notice, at 9:15 a.m., in room 556, 275 Peachtree Street, Northeast, Atlanta, Ga., Hon. Parren J. Mitchell (chairman of the committee) presiding.

OPENING STATEMENT OF CHAIRMAN MITCHELL

Mr. Mitchell. Good morning. I think we will bring the committee to order.

On behalf of my colleagues on the Small Business Committee, I welcome you to the committee's fourth field hearing. As some of you know, this hearing was scheduled for November 23, 1981, but the Congress at that point was busily engaged in something called the continuing resolution and votes were so close I dared not leave; therefore, we had to cancel the hearing that was scheduled for the 23d.

I regretted having to do that because a number of people had planned things for the committee representatives and also a number of people had worked very hard to get their testimony in to try to be here, but I had no choice. The legislative process in Washington takes precedence, always, over any other activity.

I am not a stranger to Atlanta. It is a very beautiful city, lots of construction work being done. I am well aware of the splendid leadership that the former mayor, Mayor Maynard Jackson gave, and how successful he was in promoting the growth and development of small businesses and minority businesses in this city.

I have known and worked with your new Mayor Andy Young for many years. I know he is a dedicated individual and I know that he will be a strong advocate for continuing the gains made by the small and minority business community.

Generally when we have hearings we are always rushed and we don't do things properly. There are many, many people who work behind the scenes to put on a field hearing. I want to publicly thank some of those people now: Tommy Dortch from Sam Nunn's office; Dave Miller, compliance officer for the city of Atlanta; and Lequita Booth of the Georgia Small Business Development Center did a superb job in assisting my staff with the planning for this hearing. On behalf of the committee, please accept my sincere appreciation.

In January 1981, I was elected to chair the Small Business Committee of the U.S. House of Representatives.

By the way, my name is Parren Mitchell.

That was one of my first commitments, that we would have four field hearings a year throughout the country. There were two major reasons for that choice. I have been in Congress longer than I planned to be, 11 years, and I have learned it is just too difficult for many small businessmen to come to Washington. They simply cannot afford it. The burden and expense of being away from their businesses makes that impractical. Therefore, that was one of the first reasons we decided to have a field hearing.

The second reason is that we have got to be able to go out to where people are, to get information from them as to how policies are affecting them; certainly we want to know how laws are being implemented.

It has been my very sad experience since being in the Congress to learn over the long 11 years, there is very often a big gap between what we enact into law and what is actually implemented out in the field.

The only way we can really get good information on that is to go to the field to ascertain the effectiveness of the administration carrying out the mandates of the Congress.

The Small Business Committee's work has stepped up enormously this year. There are 14 million small businesses. Many of them are in trouble in this country. There has been a decline in small business output. On the other hand, there has been a growth in large corporations. A large amount of evidence available supports the theory that economic concentration results in inflationary charges, amounting to approximately 9 percent. Small businesses are a victim of this process, but certainly the biggest victim is the consumer.

I would submit to you that we have done fairly well this year on the committee. Our bill, H.R. 4326, the Small Business Research and Innovation bill, had 130 cosponsors in the House. The bill has been passed by our committee, and we expect that bill to be passed by the full House this summer, certainly this year.

We have some concerns about the administration's overall economic recovery plan. We have had some problems, of course. I have not felt the kind of commitment to small and minority businesses that I think should be evidenced by this administration, but perhaps the testimony we elicit here will clear up that concern.

I recently received a compliment—I guess it was in one of the papers in Washington—pointing out that I was a hard-working chairman, that I tried to treat my colleagues with respect and cooperation, but the criticism was that I was overly concerned about minority business. Well, I accept that criticism.

I am enormously concerned about minority businesses. I think you can't just say all small businesses ought to be treated alike. Unfortunately there is racism along with other barriers in the free enterprise system that intrude on the minority business process. It is for that reason that we, the Congress, passed a bill, Public Law 95-507, by legislation.

This law was designed to assist and foster the development of socially and economically disadvantaged businesses. In this regard also the 8(a) program was developed as part of Public Law 95-507 to provide minority businesses with procurement and other business development assistance.

It is no great secret that the 8(a) program has been the target of extensive criticism in Washington and around the country, but that is nothing new. That criticism was evidenced from the very beginning of the concept in 1968. Problems with the 8(a) program were enhanced by some actions taken by the new Administrator, Mr. Cardenas. He announced early on in the game there would be "new tough policies for the 8(a) program," and indeed he did initiate some very tough policies, many of which I don't agree with: A moratorium was placed on the designation of new firms; any contract with a value of more than $2 million under his policy must now be approved by the Administrator; advance payment on business development expenses were also restructured.

Then in May of this year, Mr. Cardenas authorized an immediate review of all 8(a) firms alleged to be above the definition of small businesses. A total of 48 firms were found to be large businesses. It is my understanding that 20 of the 48 are appealing SBA's initial finding. I am pleased to announce that the Administrator partially lifted the administration of new 8(a) firms in October.

Unfortunately, in Seattle, New York, Washington, Cleveland, and Hartford, the moratorium is still in effect. I have urged the Administrator, Mr. Cardenas, to completely lift the moratorium.

The other problem that we encountered this year came on June 1, 1981. That was the proposed graduation regulations. A hue and cry arose all over the country. The Administrator planned to force graduate some firms from the 8(a) program and suggested that those firms stay in the 8(a) program for only 3 to 5 years. Every single member of the House Small Business Committee and the subcommittee on which I serve felt that that was wrong. There is simply no way to place that time constraint on a small business, particularly an 8(a) firm, and expect it to prosper after 5 years. As a result of that public outcry, the revisions were made and now it is proposed that there be a 5-year period with a 2-year extension and a 1-year phaseout, a total of 8 years that a firm can stay in the 8(a) program.

I still disagree with that. We have enough testimony to indicate that it takes somewhere between 15 and 20 years before a business can become viable, before it can go public and sell stock. That is a test of its viability.

I announced that we plan hearings for this year. If my blood pressure and back and all other ailments hold up, we will have four more next year. We did meet in Los Angeles and Phoenix. We were in Chicago and this is the last hearing for last year, beginning this year. We have uncovered startling information on occasion in these hearings. One common theme was that the higher interest rates were just driving small businesses out of business.

Another difficulty that was encountered was the fact that in the field people seem to believe the SBA was uncertain about its role in the guaranteed loan program. It was proposed that the guaranteed rate on those bank loans be reduced to 70 percent from 90 percent.

We heard testimony from the banks indicating they simply could not live with a 70-percent guarantee. As we have moved around, we have learned there has been a great underutilization by minority business enterprises as subcontractors by prime contractors as is required under Public Law 95-507.

We also learned that there have been failures—failure of the SBA and procurement agencies—to comply fully with the requirements of the 8(a) program. At today's hearing we will focus on a cross-section of problems and opportunities affecting the small and minority business community.

Since the new administration has come in, it has moved to implement what it proposes as a new economic recovery program. Small and minority business changes in government have been instituted. We have had deep agency cuts in the Small Business Administration. We have had business tax cuts on the other hand.

In light of all these changes, I believe it is imperative that the Congress and especially this committee begin a systematic investigation of the impact of these broad new policy directions on the small and minority business sector and also the ability of the Federal agencies to carry out these new policies.

I am delighted that Congressman Newt Gingrich is here with us. How long have I known you now?

Mr. GINGRICH. Four years.

Mr. MITCHELL. We are not always in philosophic agreement but I think we are good friends. It is kind of you to take the time to be with us. I expect Congressman Hatcher will join us. He is in one of the local hotels where they are having water problems, no water in his room at all. His staff is here. Let's hope that that will work out.

I wanted to introduce on my right Major Clark, who is the staff director for the Small Business Committee, and Steve Blackistone, who is the minority counsel for the Republican side on the Small Business Committee.

I further understand that Congressman Wyche Fowler has a representative here.

Mr. JACKSON. Thank you, Mr. Chairman.

Mr. MITCHELL. He is in the Far East, I believe?

Mr. JACKSON. Yes. He does have a prepared statement. I will be delighted to submit that.

Mr. MITCHELL. We will hear from Congressman Gingrich. Maybe by that time Congressman Hatcher will be here.

Mr. Jackson, could you come up and present the statement from Congressman Fowler?

TESTIMONY OF CHARLES JACKSON, ON BEHALF OF HON. WYCHE FOWLER, JR., A REPRESENTATIVE IN CONGRESS FROM THE STATE OF GEORGIA

Mr. JACKSON. Mr. Chairman, Congressman Gingrich, other members of the committee, I am Charles Jackson. I manage Mr. Fowler's office here in Atlanta. I am delighted to welcome you to our great city.

You will be hearing today from some of the people who have been responsible for this city's great and dynamic growth over the last two decades. We think that Atlanta is an excellent place to look for clues to the state of small business in America today, because small businesses have been the driving force behind much of this city's exciting growth and development.

It might well be appropriate to declare Atlanta the minority enterprise capital of the world, because Atlanta has more able, energetic, and successful black businessmen and women per square inch than any other city in the world. So you have come to the right place.

I hope you will listen well. Like the rest of America, small and minority businesses in Atlanta are staring into a double-barreled shotgun, one barrel loaded with recession, the other with budget cuts in programs vital to their success.

In the fiscal year ending June 30, 1981, bankruptcy filings in the northern district of Georgia jumped from 6,357 to 8,786, a 38-percent increase. And, although it may be in some measure testimony to the relative strength of small businesses in Atlanta, it is nevertheless appalling to note that bankruptcy filings throughout the Nation swelled by 44 percent over the same period.

When the Reagan administration steamrolled its budget package—which among other things cut SBA funding by 37 percent—through Congress last summer, they neglected to explain, publicly at any rate, that their plan to squeeze inflation out of the economy called for a recession calculated to squeeze thousands of small businesses into bankruptcy.

America needs small business. Some 80 percent of all new jobs are provided by small businesses. Minority businesses and small businesses generally offer the best hope we have of solving the chronic unemployment problems among minorities and young people.

Small businessmen are the risk-takers in our economy, and risk-taking is necessary for economic growth and vitality. Unfortunately, sensible risk-taking requires confidence in the economy, and the confidence is just not there right now and for good reason, as David Stockman has recently disclosed.

The pieces won't fit. The tax cut is weighted too heavily toward big business, and it went too far too fast. Huge deficits guaranteed by Kemp-Roth, coupled with an uncompromising policy of tight money, looks very much like a prescription for disaster for small business.

With the darkening clouds of recession hanging over us, now is no time to turn our backs on the highly successful programs designed to help small and minority businesses.

I commend you, Mr. Chairman, for your aggressive leadership in confronting these problems, and I pledge to you and my friends here today my full support in finding, and funding, appropriate solutions.

Thank you.

This ends Mr. Fowler's statement.

Mr. MITCHELL. Thank you very much. We thank Congressman Wyche Fowler for his statement.

[Attachments to Mr. Fowler's statement follow:]

SMALL BUSINESS ADMINISTRATION BUDGET COMPARISONS

	Direct loans (millions)	Loan guarantees (billions)
Fiscal year 1981 appropriations	$367	$4.5
Fiscal year 1981 actual expenditure	333	3.4
President's March request for fiscal year 1982	260	3.15
Reconciliation	230	3.3
SBA interpretation of President's Sept. 24 request	200	2.8

Note: Information supplied by Thomas Powers, general counsel, Small Business Committee.

BANKRUPTCY FILINGS

	Year ended June 30, 1979	Year ended June 30, 1980	Year ended June 30, 1981	Percent increase 1981 over 1980
United States nationwide	226,476	360,957	519,063	43.8
Northern District of Georgia	4,734	6,357	8,786	38.2

Note: Information supplied by the Administrative Office of the U.S. Courts, bankruptcy division.

Mr. Jackson. Thank you, Mr. Chairman.

Mr. Mitchell. Mr. Dortch, you were not in the room when I praised you to the skies.

This is Mr. Tommy Dortch of Sam Nunn's office. Thank you for the assistance and help you have given us.

One other housekeeping announcement before we hear from Congressman Gingrich. There are additional copies of testmony over there, and you may help yourself to copies of the additional testimony. Please help yourselves. There is quite a load to take back on the airplane, so don't have any hesitancy at all in taking extra copies of the testimony.

Congressman Gingrich, do you have an opening statement?

OPENING STATEMENT OF HON. NEWT GINGRICH, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF GEORGIA

Mr. Gingrich. Let me first of all thank you, Congressman Mitchell, for bringing this hearing to Atlanta and for allowing us to have the opportunity to have local businesses and local communities talk with you and present testimony.

Let me remind the Atlanta community that you have been a real leader. I've learned a great deal from you in the last 4 years. You, along with Augustus Hawkins, have emphasized that the key to ending the cultural poverty in America is minority enterprise opportunities that translate into new jobs. I am delighted that you are chairman of the Small Business Committee, and I commend you for the work you have done in your first year as chairman.

I am concerned about all small businesses, but I want to focus today on two areas: First, minority enterprise. I want to reinforce Congressman Mitchell's earlier points. Racism does exist. The scars of a welfare culture and segregation continue to cripple minority enterprise and minority entrepreneurs. And no single change could end more poverty and create healthier inner cities than a flourishing, successful minority business community.

I note Bob Wright is in the audience today. Bob and I have been working on the problems of minority enterprise since 1972. It's a crucial area we have to address. Furthermore, while I am glad to see Georgia Pacific and other corporations move to Atlanta, I think it is far more important that we have an explosion of the minority enterprises that already employ 19,000 people in the Atlanta area; the doubling or tripling of the size and strength of those minority enterprises would do more to create a healthy Atlanta than would bringing in every corporate enterprise.

Second, we need to recognize a new class of businesses, what I call baby businesses. A friend of mine who is a former English teacher turned auto mechanic went into business for himself. I approached him to get advice for Mr. Mitchell's committee. He said, "I am too small to be a small business. Everything I have looked at for small businesses is one leap above what I have to do to survive."

In talking with Roy Richards, at the other end of the scale, the founder of Southwear Corp., a first generation entrepreneur, made the same point as Jamey Jones. He said the tragedy of American life for the last 20 years has been when little-bitty businesses get founded and are weak and fledgling and don't know what they are doing, we don't put them in a nursery, or encourage them to see what they are doing. Instead, we throw them out in the jungle to see if they can survive.

We need to have a national "baby business bill" that would say something like this: From the time you are founded until you are either 5 years old or have at least 10 employees, we are going to put you in a legal nursery. You are going to pay dramatically lower tax rates; don't fill out any forms except those necessary to meet Federal taxing requirements; nobody will bother you and ask you to be a volunteer bureaucrat. Just go out and make money to survive and prosper. Something like this would have a great effect in the black community and on minority enterprise generally.

We have to let banks take a 2- or 3-percent tax credit for loans made to people who fit that category. I am not sure of the details. I simply suggest this to you. Nothing will help America more than to find a way to cut through the whole scale of hurdles that currently say to a young teacher at Georgia Tech or Morris Brown, "Don't go out and found a new business; it's not worth the effort."

Let me, in closing, say that we are at the edge of a shift, a move away from a welfare state that, for example, attempts to help some small businesses by narrowly focusing bureaucracy in such a way that not more than a relative handful of all the 14 million small businesses get Government help.

I think we have to move toward what I've been calling an "opportunity society," one which says that we'll change the rules of the game to help small businesses, but afterward men and women have to go out on their own, learn those rules, and help themselves.

It is impossible with just Federal aid to help enough small businesses to be fair to all 14 million of them. It is possible to set up a new set of rules and a new set of policies so everyone who has the courage to try to be successful and creative can have the maximum opportunity to succeed and flourish.

I pledge myself to work closely with Congressman Mitchell in his work to build a track record in small business. That will encourage a new generation to create jobs so all Americans have a chance to make a living.

Mr. Mitchell. Thank you for taking your time. This is, I hope, demonstrable evidence to the critics of the Congress who say we take vacations when the Congress is not in session. We don't. We work most of the time, and work very hard. I know it must be at some cost to you, Newt, to take time to be here.

Mr. Gingrich. I am delighted to do it.

Mr. Mitchell. I think I covered all the announcements. One other thing. There was overwhelming interest—our phones were ringing in Washington about participating in the hearing. I think people will be coming in. I would assume a number of people are attempting to recover from the warm weather last week when those tropical storms hit Atlanta, and Georgia, and South Carolina. So some people are having some difficulty getting here. I can appreciate that.

Our first witness will be Mr. Miller Widemire, Regional Administrator for the U.S. Small Business Administration for region IV.

TESTIMONY OF MILLER WIDEMIRE, REGIONAL ADMINISTRATOR, SMALL BUSINESS ADMINISTRATION, REGION IV, ACCOMPANIED BY WILEY MESSICK, DEPUTY REGIONAL ADMINISTRATOR; DAVID L. COKER, REGIONAL COUNSEL; MERRITT SCOGGINS, ASSISTANT REGIONAL ADMINISTRATOR, FINANCE; ISAIAH WASHINGTON, ASSISTANT REGIONAL ADMINISTRATOR, MINORITY SMALL BUSINESS/CAPITAL OWNERSHIP DEVELOPMENT PROGRAM; JOHN P. LATIMER, ASSISTANT REGIONAL ADMINISTRATOR, PROCUREMENT; AND ROBERT WRIGHT, ASSOCIATE ADMINISTRATOR, MINORITY SMALL BUSINESS/CAPITAL OWNERSHIP DEVELOPMENT PROGRAM

Mr. Widemire. Mr. Chairman, may I have an opportunity to introduce my staff that is with me today and some visitors? First off, not a member of my staff—I am a member of his staff—Dr. Wright from Columbus who heads up the minority small business/capital ownership development program in Washington. We are delighted to have him with us.

I am delighted that we still have the services of Wiley Messick, whom I am sure you and all of your staff have known for years, as Deputy Director; my general counsel, Mr. Dave Coker; Merritt Scoggins, who heads up our Finance Division; and Mr. Isaiah Washington, who has the longest title of all, Assistant Regional Administrator for minority small business/capital ownership development.

Mr. Mitchell. Is the power concentrated in him commensurate with the length of his title?

Mr. Widemire. Absolutely, without a doubt. That power is considerable in view of the fact I have been on board 3 months and I think I have seen Mr. Washington 3 days during 3 months. He has been in Washington working so much with Dr. Wright on the program.

Mr. Chairman, is it your pleasure that I should read the statement?

Mr. MITCHELL. You have an option. You can present your statement in its entirety or you can submit it for the record and merely highlight various points of your statement. Either option you care to pursue.

Mr. WIDEMIRE. If it should suit the chairman's convenience then, I believe it will take me 15 or 20 minutes to read it, if that is not too long.

Mr. MITCHELL. That is all right.

Mr. WIDEMIRE. I might stop and digress for a moment or two to highlight some points during the written part, if I may.

Mr. MITCHELL. Sure.

Mr. WIDEMIRE. Fine.

Mr. Chairman, members of the committee, I appreciate the opportunity to appear before you at this hearing. I am just completing 3 months as the Administrator of SBA's programs in this region, although I have had extensive experience in operating a small business and in providing professional services both to active small businesses and to small businesses in liquidation.

At first hand I have had opportunities to observe successful and unsuccessful small business management. Because of these experiences with small businesses, I believe I can provide effective leadership to the delivery of SBA services to the small business community in region IV and, at the same time, protect the interests of the taxpayers in regard to SBA programs.

There are eight Southeastern States in region IV, the coastal States from North Carolina to Mississippi, and the inland States of Tennessee and Kentucky. There are nine district offices in the eight States. Florida is the State with two districts, Jacksonville and Miami. We have one branch office, Biloxi, opened to serve the Hurricane Camille disaster loans and now also serving the Mississippi portions of the Hurricane Fredric portfolio. In addition, there are six post-of-duty stations in region IV.

The region has been characterized in recent years by steady growth in manufacturing and service businesses. The historic migration of both unskilled and highly trained citizens to other parts of the country declined in the seventies and has been offset in part by return of many people born in the region and by migration of others to the Sun Belt both for retirement and for new employment opportunities.

Opportunities for small businesses are still extensive in this region. Although large firms have major economic significance in textiles, pulp and paper, steel, and general manufacturing, and in transportation, distribution, and retailing.

On the subject of the farm disaster loans, Mr. Chairman, a review of the activities of SBA in region IV might well begin with a report on the farm drought disaster loans made under the Administrator's disaster declarations of 1977 and 1980 following severely dry weather over most of this region in those years. Certainly the lending activity under those declarations and the resulting loan collection responsibilities dominate the personnel resources of this region.

Prior to 1976, the Small Business Act did not permit any loans to agricultural enterprises. In that year the act was amended to permit SBA to make agricultural loans. Even after the statutory change, SBA did not make agricultural disaster loans because the Department of Agriculture had the programs, the budget, and the expertise.

If I might add to my prepared statement, they also had the personnel.

SBA believed that it would be better for the farmers and more cost-effective for the Government if the Department of Agriculture carried out these functions.

In the spring of 1977, when the extent of the drought in the South and Midwest became apparent, SBA—under intense pressure—opened the disaster loan program to farmers. It was in this setting, and with no prior experience, that SBA began its disaster farm lending program.

There was much for the agency to learn, but little time in which to learn it, since the program came into being in the midst of a serious drought. All the while that SBA was developing the program, there was intense pressure to get the money flowing. And this the agency did. The program level increased tenfold, from about $200 million a year to over $2 billion a year.

Since that time SBA has made many changes to correct various problems that emerged during the first year of the program. As SBA has gained experience, its regulations have been changed to reflect the agency's understanding of the economics of farming. Particularly, SBA has changed its methods for identifying the amount of losses, setting terms for disbursement, drawing loan terms and conditions and insuring that duplicate assistance is not forthcoming. Finally, Public Law 96-302 has attempted to put the responsibility for providing farm disaster assistance back in the Department of Agriculture, where it belongs.

The entire loan portfolio of the region was approximately $1 billion at the time of the 1977 declaration. A year later the portfolio was over $2 billion, with just over $1 billion having been approved under the 1977 farm declaration—$400 million by the Georgia district office alone. Farm loans approved under the 1980 declaration have exceeded $300 million in the region and additional loan increases are being made now under legislation passed in late fiscal year 1981.

The portfolio at the end of fiscal year 1981 stood at 68,000 loans for $2.885 billion. Disaster loans accounted for more than half of the portfolio. These are all direct loans, requiring collection by SBA personnel. We cannot look to banks or any part of the private sector for collection of these loans under current law.

If I may address a remark as to that, to put that in scope for your committee, I am informed that compared to 10 years ago, the SBA personnel of this region are producing and working at the level, according to which program you look at, from 150 to 250 percent of productivity of 10 years ago, with virtually the same number or less people than 10 years ago. That sort of gives you some idea of what has transpired and how really more productive personnel of this region are.

In connection with that, we have welcomed the addition of 99 temporary employees that Administrator Cardenas announced for region IV collection activities during the fall of 1981, hearings by the Senate Committee on Small Business. The highest priority of the new temporary employees is to review the files for loans or portions of loans which duplicate the benefits from Department of Agriculture agencies. Their services are also being utilized in general collections of the large volume of outstanding farm loan dollars.

As I mentioned earlier, about one-half of the portfolio is in farm loan dollars.

Last winter and spring, the region had as many as 5,000 delinquent farm loans. Although farm production is up this crop year, the 1981 crop year, most farm commodity prices are substantially below last year's prices. We may reasonably expect 3,000 to 6,000 delinquent farm accounts between February 1 and April 1. Furthermore, many of the accounts will be kept or brought current only by the time- and talent-consuming process of subordinating SBA real estate loans to annual crop production loans by the Production Credit Administration and other 1982 crop lenders. I understand that at planting time in the spring of 1981 all Atlanta district office collection employees—all loan servicing and collection people, permanent and temporary, were involved in the processing of subordination actions for several weeks.

Mr. Chairman, in some SBA regions and districts, disaster loan activity remains a secondary responsibility, but in this region in recent years, it has been the primary responsibility. With the help of legislation that has returned nearly all future farm disaster lending to the Agriculture Department and in the hope that 1982 brings no more flood, tornado, and hurricane activity to the region than has 1981, I expect to be able to focus more regional and district management attention on the traditional SBA program areas of financial, management, and procurement assistance, with special emphasis on the minority business programs and delivery of SBA services to other target groups, such as women, veterans, and the handicapped.

On the subject of the 8(a) program, at this point I would like to review the work of the region's Minority Small Business and Capital Ownership Development Division. The 8(a) program in region IV has grown steadily each year, as reflected in exhibit I. Activity grew from 215 contracts for $57,729,030 in fiscal year 1977 to 328 contracts for $132,925,184 in fiscal year 1981. Currently there are 200 8(a) firms in the region's portfolio. Exhibit II, Mr. Chairman, gives a State-by-State breakdown. In fiscal year 1981, section 7(j) call contractor assistance was supplied to 308 firms—255 minority firms—through the MSB/COD administered programs.

During recent years, the MSB/COD division has worked extensively and successfully to bring about significant 8(a) program improvements, some under legislation, some by administrative action directed from the central office, and some by internal improvements in procedures and practices by the division. The improved administration has been so noteworthy that both the previous agency leadership and present leadership have called on our Assistant Regional Administrator, Isaiah Washington, for extended duty in key management places in the central office.

With Mr. Cardenas' recent lifting of the moratorium on new applications for 8(a) program entry, we have processed 25 applications in the last several weeks. However, our rate of adding more firms to the 8(a) portfolio will be limited by two factors. First, personnel limitations require that the number of new entrants bear a reasonable numerical relationship to the number of firms leaving the program as successful graduates or unsuccessful dropouts. Second, we are under the legislative mandate of Public Law 96-481 to establish fixed periods of time for program participation for each company in the program and this administrative work with each firm must be completed by April.

Dr. Robert Wright, the Assistant Administrator for the Minority Small Business/Capital Ownership Development, is scheduled to meet with our region IV 8(a) contractors January 26 here in Atlanta. I plan to be there to meet with as many of these 8(a) contractors as is possible and have many of our staff there.

On the subject of surety bond guarantees, region IV continues to lead the Nation in volume of surety bond work. Approximately 30 percent of surety bond guarantee activity has occurred in this region since the program's inception and the region's default rate has been less than 2 percent and usually about 1 or 1½ percent. Exhibit III, with chart attached, reflects the region's surety bond guarantee activity by districts for fiscal years 1980 and 1981.

To put that in perspective, Mr. Chairman, our regional share of the Nation would be roughly 10 percent—10 to 12 percent share, where we have produced approximately 30 percent, though, of the Nation's business in this area, of some good quality, we are proud to say.

In the area of management assistance, in the management assistance program, exhibit IV, SBA personnel and the leveraged resources of the Service Corps of Retired Executives and the small business institute program provided management counseling to 23,113 firms. Of this counseling, 32 percent was to minority businesses, 38 percent to women-owned businesses and 5 percent to exporters.

In addition, small business development centers, funded substantially by SBA, counseled 6,123 small business clients. SBA and SCORE and cooperating organizations and institutions provided management training to 38,943 people, 32 percent to minority citizens, and 46 percent to women. The SBDC's trained 15,461 additional business people or prospective business people.

In this region six of the eight States have SBA approved and partially SBA funded small business development centers. The centers begun at the University of Georgia and West Florida University have been very strong. These established many of the SBDC prototype activities and procedures and developed good statewide networks. The South Carolina SBDC is developing a strong program. Alabama's SBDC shows promise after a slow start. The Mississippi and Kentucky SBDC's are new, but indications are that they will serve their States well, too.

The figures shown on exhibits V and V(a) are slightly different for the totals, about $5 million. That arises, Mr. Chairman, because one is based on our cuff notes and one is based on the official computer results, so there is that slight little variation there.

Mr. **Mitchell**. A $5 million variation?

Mr. **Widemire**. Only out of $448 million. What is that, one-half of 1 percent? It probably arises by when the computer dated it in and when we were dating it in, that last little stretch at the end of the year. I am sure that accounts for the slight difference.

Total minority loan activity of $42,010,000 in fiscal year 1981, $40,788,000 in fiscal year 1980 and $38,999,000 in fiscal year 1979 is separated into direct and guaranty volume in exhibit VI.

Region IV is firmly committed to the administrator's goals of improving the quality of SBA's loans and strengthening the effectiveness of our collection activities. I can already, and do, see an overall improvement in the quality of our new loan approvals.

The region's loan portfolio of 68,000 loans for $2,885 billion presents an enormous challenge to district and regional management. At the end of fiscal year 1981, 77.54 percent of the region's portfolio was current—exhibit VII—as compared with a target rate of 82-percent current loans. Even the target figure represents a substantial drop from expectations in the first half of SBA's 28-year history. Although farm loans make up a heavy portion of the delinquent loans, business loans and economic opportunity loans also have higher than historic delinquency rates for this region.

If I may make a comment beyond the printed record, our region, as low as that currency rate is, still stands pretty well with the Nation as a whole. We are pleased with that.

We are beginning to see improvement in that, even though small businesses are continuing to have harder times. As we have these additional people, they are beginning to have early results. We are beginning to see some. We are delighted with that.

Mr. Chairman, in the area of procurement assistance, the procurement assistance programs in region IV are doing very well.

If I could refer you to page 9 of the printed statement there, without going through this, reciting these figures, I do want to change one figure, because it is pretty significant. In the summary figures on page 9, the second line, the percentage should be 78-percent increase.

I would just comment on that series of figures for the chairman. The total awards in 1981 compared to 1980 in dollar amounts are doubled, but I think it highly significant that of the total awards, our percentage to small business has grown from 18.4 percent to 20.53 percent.

[Figures referred to above follow:]

Prime Contracts—Summary

Total contract dollars issued 1980, $5,584,256,060;
Total contract dollars issued 1981, $9,921,376,000—a 78 percent increase;
Total awards to small business 1980, $1,027,421,294 or 18.40 percent;
Total awards to small business 1981, $2,037,343,000 or 20.53 percent;
Total set-asides to small business 1980, $508,217,923 or 9.10 percent; and
Total set-asides to small business 1981, $1,028,660,000 or 10.36 percent.

Mr. **Widemire**. That is a pretty substantial percentage jump of the totals and a doubling in dollars, in raw dollars. The set-asides to small business have more than doubled in that year, and the percentage of the total has gone from 9.1 percent to 10.4 in round percentages.

We are very, very encouraged about that, and we are delighted with that trend. We are going to try our best to keep that up.

We have a new position in region IV termed a "breakout" procurement center representative, and the incumbent is located at Warner Robins Air Force Base. His efforts in 1981 resulted in $36,690,000 more in procurement for small business. This is one person, Mr. Chairman. This individual, with an engineering background, works back in the drawing board area, screens drawings for parts that can be made by small businesses, and requests that the parts be coded so that small businesses will get the bid package or the procurement will be set aside.

I am informed that the three breakout PCR's in the country have saved the Government $6,700,000 in 1 year in documented and audited studies—equivalent to $2,223,000 per PCR. This obviously is a very promising program.

Region IV significantly improved its prime contract assistance to small business this past year.

In the area of certificates of competency, in fiscal year 1981 we approved 51 businesses as being capable of performing a specific contract after the procuring agency had determined the business incapable. Of the 51, only one company is delinquent in on-time delivery. By certifying that those low bidding small companies were capable of performance, we saved the Government $1,514,881 between the bids of the COC recipients and the next low bidders on these 51 procurement actions.

If I may add to the record, we feel very good about the very low delinquency rate. Where we are certifying that they are competent, they are turning out to be. We are very pleased with that record.

In the area of procurement automated source system, PASS is a comparatively new system from the standpoint of acceptance and utilization. With the quantum growth in business diversification and the development of new businesses, PASS is a great innovation in the collection and storage of sources of businesses for bidding on Government contracts. The utilization of this system by Government procuring agencies and private industry should be encouraged by those in positions of authority and influence. There are 60,042, businesses listed in the system now and we are adding approximately 2,000 per month. Of the 60,042 we have registered 6,324 from region IV.

On the subject of technology assistance, this program was designed to assist small businesses with problems related to high technology and also to make available to small businesses advances in the state of the art or new products and ideas that result from Government-sponsored research and development. We solicit inquiries through conferences, individual counseling, workshops, newspaper releases, and reader service cards in technology magazines. The reader service cards are usually placed on a national basis and initiated by Washington office personnel. Our goal this year is to process 152 cases involving technology transfer or assistance. We handled 158 cases last year against a goal of 150.

On the subject of size determination, if a procurement is set aside for small business only, there is a space in the procurement package for the business to self-certify that it is small. If the contracting officer or another bidder thinks the low bidder is a large business, a formal protest may be filed with the contracting officer within 5 days after award has been announced. The protest must be timely and it must cite specific facts supporting the allegation.

The contracting officer must assert the protest to the regional office in which the protested company or its corporate headquarters is located. If the protest does not adequately specify grounds for the protest, SBA will summarily dismiss the protest allowing the procuring activity to proceed with an award. If we accept the protest, we immediately make a request to the company for information concerning number of employees, sales, dollars, stockholders and their relationship to other businesses, subcontracts, and indemnifications on bonding. From this information, which is certified, we make a determination and issue a decision. There is an appeal from a regional size determination. The appeal can be made by anyone adversely affected by the decision and is made directly to Small Business Size Appeals Board, SBA, Washington office. We are required by law to process size determinations within 10 days; however, extensions are granted. We do not have a goal assigned to this activity.

In the area of subcontracting, results of the region's work in behalf of subcontracts for small businesses, disadvantaged small businesses, and women-owned businesses are summarized in exhibit VIII.

If I may for the record, for those who may have picked up a copy off the desk, the very last page of the whole portfolio should be the first page of exhibit VIII. It is the summary page. The other four pages of exhibit VIII simply give the breakdown.

Mr. Chairman, after what, I am told, was a slow start on subcontracting responsibilities under Public Law 95-507 by Government and industry, SBA is doing its best to increase significantly the positive results under the legislation which you and Senator Nunn of Georgia guided through the 95th Congress. We will continue to press for effective responses in behalf of small and disadvantaged small businesses by prime contractors and other Government agencies in region IV.

At the close of fiscal year 1981, region IV had 24 prime contractors holding contracts subject to surveillance under Public Law 95-507. These companies also volunteered for SBA to review their entire subcontract programs to small business. In fiscal year 1982, region IV has added 16 companies that participate in a review of their entire subcontract program.

Thank you for the opportunity to report to you on the work of this SBA region and the challenges and opportunities before us. Members of my staff and I are available for your questions.

[Attachments to Mr. Widemire's testimony follow:]

MSB & COD
Section 8(a) Contract Activity
1977 – 1981
Region IV
Small Business Administration

	FY - 1981		FY - 1980	
District Office	# of Contracts	$ Amount	# of Contracts	$ Amount
Atlanta	95	$ 37,814,536.54	125	$ 37,115,749.00
Birmingham	55	23,765,442.44	63	18,408,062.00
Charlotte	36	20,583,523.93	49	34,112,452.00
Columbia	25	18,056,714.67	40	16,248,377.00
Jackson	20	6,955,245.32	18	2,346,966.00
Jacksonville	16	3,108,468.87	20	6,187,689.00
Louisville	20	6,957,825.70	26	3,340,610.00
Miami	24	3,352,794.49	27	3,465,435.00
Nashville	37	12,330,632.12	31	6,638,688.00
Totals	328	$ 132,925,184.08	399	$ 127,864,028.00

MSB & COD
Section 8(a) Contract Activity
1977 - 1981
Region IV
Small Business Administration

	FY - 1979		FY - 1978	
District Office	# of Contracts	$ Amount	# of Contracts	$ Amount
Atlanta	73	$ 30,956,382.00	55	$ 15,750,569.00
Birmingham	33	8,008,232	31	14,095,112.00
Charlotte	68	17,354,925.00	48	17,518,986.00
Columbia	31	23,175,353.00	32	8,599,932.00
Jackson	12	979,771.00	11	1,377,579.00
Jacksonville	9	2,724,574.00	27	5,056,491.00
Louisville	12	1,565,638.00	11	1,434,452.00
Miami	13	2,961,963.00	7	1,834,935.00
Nashville	23	5,425,213.00	34	7,191.704.00
Totals	274	$ 93,152,051.00	256	$ 72,859,760.00

MSB & COD
Section 8(a) Contract Activity
1977 – 1981
Region IV
Small Business Administration

FY - 1977

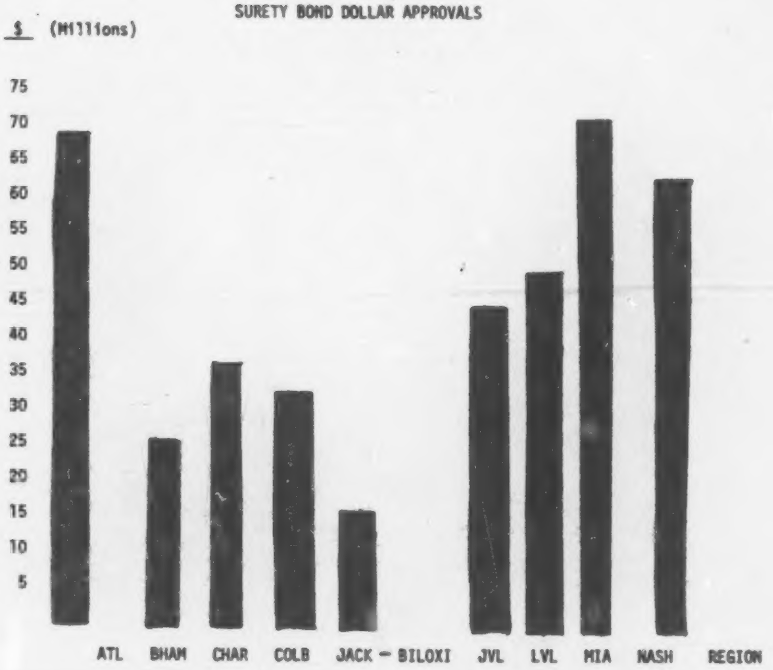
District Office	# of Contracts	$ Amount
Atlanta	39	$ 7,162,528.00
Birmingham	31	15,588,994.00
Charlotte	36	14,034,956.00
Columbia	14	7,215,646.00
Jackson	9	985,797.00
Jacksonville	23	3,363,540.00
Louisville	13	1,991,330.00
Miami	16	2,629,280.00
Nashville	34	4,756,959.00
Totals	215	$ 57,729,030.00

MSB & COD
8(a) Portfolio
Region IV
Small Business Administration

Atlanta	47
Birmingham	27
Charlotte	26
Columbia	19
Jackson	17
Jacksonville	20
Louisville	11
Miami	12
Nashville	21
Total	200

REGION IV

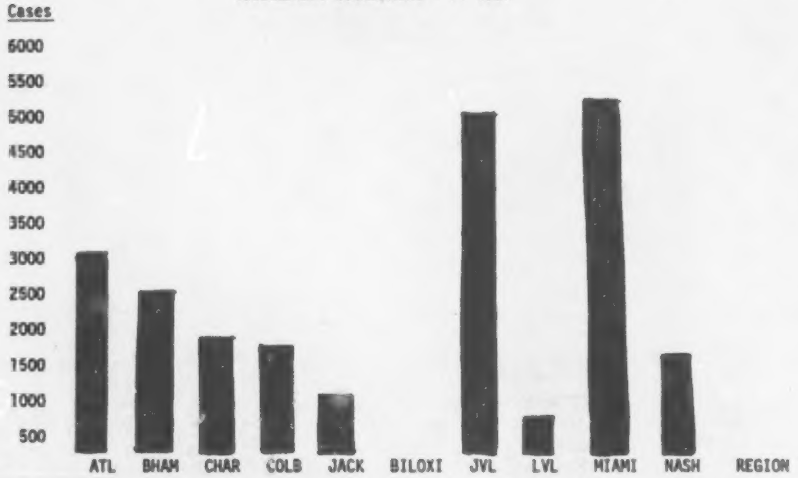
SURETY BOND DOLLAR APPROVALS



	ATL	BHAM	CHAR	COLB	JACK	BILOXI	JVL	LVL	MIA	NASH	REGION
TOTAL '81	68.7	25.4	36.4	33.0	15.3	-	44.3	48.4	71.1	63.7	399.3
'80	85.5	28.9	27.0	35.7	12.4	-	50.8	44.7	70.4	69.9	425.7
% Change	-20%	-12%	+35%	-7%	+23%	-	-13%	+8%	+1%	-9%	-6%

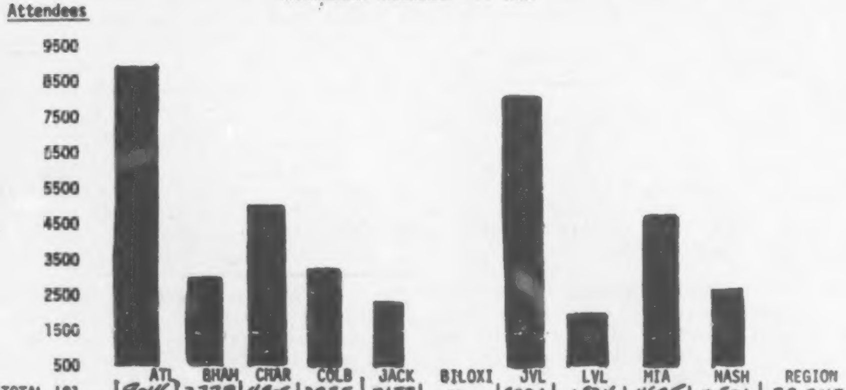
REGION IV

MANAGEMENT COUNSELING - FY 1981



	ATL	BHAM	CHAR	COLB	JACK	BILOXI	JVL	LVL	MIAMI	NASH	REGION
TOTAL '81	3151	2516	1931	1735	1082	—	5011	829	5333	1585	23,113
'80	4333	1570	3021	1894	1055	—	5054	1400	5463	1724	25514
% CHANGE	-27%	+60%	-36%	-9%	-2%	—	nc	-41%	-2%	-8%	-9%

MANAGEMENT TRAINING - FY 1981



	ATL	BHAM	CHAR	COLB	JACK	BILOXI	JVL	LVL	MIA	NASH	REGION
TOTAL '81	9046	2779	4805	2935	2137	—	8221	1824	4695	2501	38,943
'80	11593	1720	3748	2783	1610	—	6446	1517	4525	2197	36,139
% CHANGE	-22%	+61%	+28%	+5%	+33%	—	+28%	+20%	+3%	+14%	+8%

U.S. SMALL BUSINESS ADMINISTRATION
REGION IV
1375 PEACHTREE ST., N.E., 5th FLOOR
ATLANTA, GEORGIA 30367

Date: October 9, 1981

Reply to Attn of: ARA/FM

Subject: LENDING - FY 1981

To: All District Directors
Biloxi Branch Manager

Our unofficial figures on lending activity for fiscal 1981 are enclosed. It has been an interesting year. We began the first quarter with an explosive period because interest rates receded temporarily. It turned out to be the heaviest loan demand time in the history of Region IV and we ended the quarter at 180 million dollars in loan activity. We did not realize it then but that was to represent 40% of our total loan activity for this fiscal year.

The second quarter saw interest rates rise again and also brought the March guaranty reduction by the agency, but we ended the quarter with 120 million in loan approvals - the last two quarters have been very low demand periods as interest rates remained at an all time high and August was the slowest month we have had since October of 1976. We completed the year unofficially at 448 million dollars in loans which will probably rank us in the top three regions in the country.

Of course we all are aware that the lending goals of the agency were cancelled back in March - notwithstanding this we have still had an overall productive lending year. The volume in Atlanta was again heavy and that office continued to rank first in loan approvals. The new kid on the block this year has been Charlotte - this office moved aggressively into second position in the region topping over 50 million dollars, which is a record for North Carolina.

I must confess some disappointment in our CLP volume. The tight funding on guaranty lending which began in March naturally had an adverse impact on this program. We put an additional 59 banks in the program this year, and with the 49 banks already in, some gains were expected. The total volume for CLP lending was again about 19% of GP dollars for the year - same as FY 1980. If the banks want to be in this program then we have got to encourage them to use the processing procedure. I think it is clear that the Administrator will be looking to further expansion of CLP in FY 1982 and more volume from the program.

Merritt E. Scoggins
Assistant Regional Administrator
for Field Management

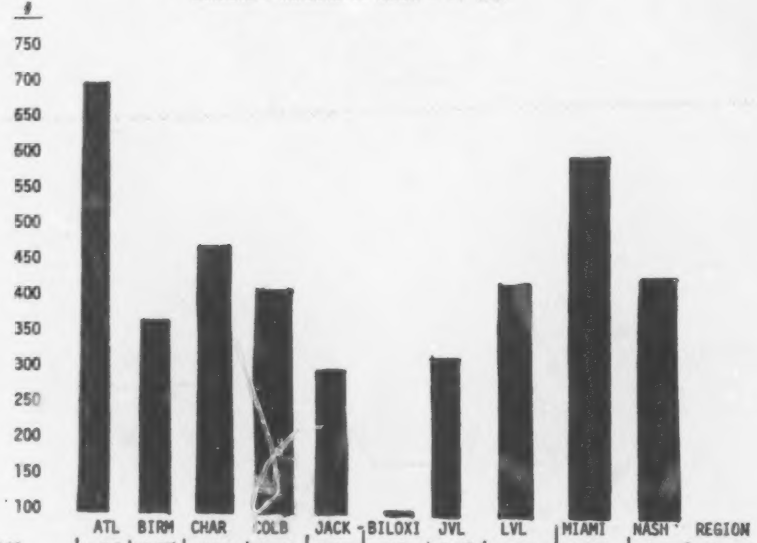
Enclosure

LENDING - FY '81 REGION IV FY THRU (SEPTEMBER, 1981)

GOAL CATEGORY	ATL	BHAM	CHAR	COLB	JACK	JVL	LVL	MIA	NASH	REGION	GOALS	PERCENT ACCOMPLISHED
DIRECT												
$Approvals	$7,011	$3,606	$3,121	$3,423	$5,819	$2,174	$2,246	$5,915	$2,482	$35,798		
%Minority ($)	34%	55%	70%	65%	37%	57%	41%	71%	38%	51%		
%Women ($)	37%	39%	29%	25%	21%	33%	28%	23%	24%	29%		
GUARANTY												
$Approvals	$88,295	$35,885	$50,331	$39,111	$31,988	$36,609	$44,504	$42,344	$43,231	$412,307		
%Minority ($)	6%	2%	7%	6%	2%	5%	1%	10%	6%	5%		
%Women ($)	9%	5%	3%	14%	8%	2%	3%	16%	8%	8%		
%MBR ($)	15%	1%	10%	16%	18%	15%	2%	1%	14%	10%		
CLP VOLUME (%)	10%	9%	33%	18%	22%	24%	19%	13%	29%	19%		
TOTAL LENDING ($)	$95,306 (1)	$39,491 (7)	$53,452 (2)	$42,534 (6)	$37,807 (9)	$38,783 (8)	$46,750 (4)	$48,259 (3)	$45,713 (5)	$448,105		

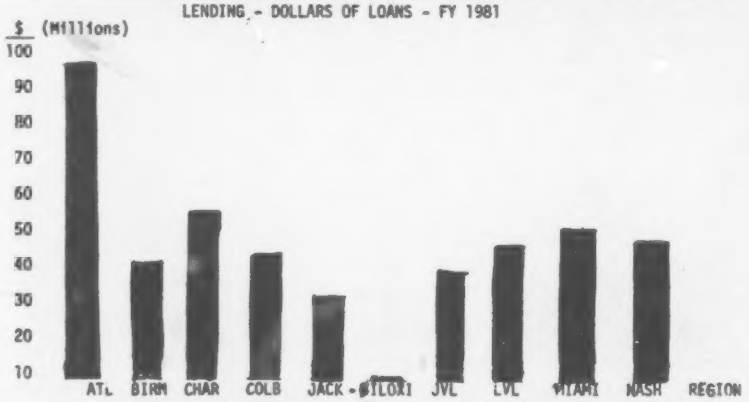
REGION IV

LENDING - NUMBERS OF LOANS - FY 1981



	ATL	BIRM	CHAR	COLB	JACK	BILOXI	JVL	LVL	MIAMI	NASH	REGION
TOTAL '81	693	354	467	404	297	76	318	407	596	410	4022
'80	699	303	485	428	311	81	338	417	646	466	4,174
% CHANGE	n/c	+17%	-4%	-6%	-4%	-6%	-6%	-2%	-8%	-12%	-4%

LENDING - DOLLARS OF LOANS - FY 1981



	ATL	BIRM	CHAR	COLB	JACK	BILOXI	JVL	LVL	MIAMI	NASH	REGION
TOTAL '81	96.1	40.5	54.2	43.5	30.4	7.3	39.4	46.7	50.9	47.0	455.4
'80	94.4	35.0	47.8	44.9	28.7	5.5	36.1	48.2	57.6	52.3	450.0
% CHANGE	+2%	+16%	+13%	-3%	+6%	+33%	+9%	-3%	-12%	-10%	+1%

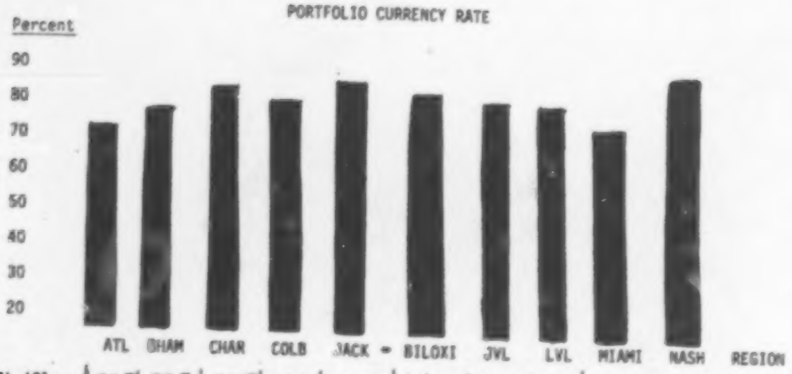
MINORITY LENDING - THREE FISCAL YEARS (79-80-81)

	NUMBER OF LOANS	PERCENTAGE OF TOTAL LOANS	DOLLARS OF LOANS	PERCENTAGE OF TOTAL DOLLARS
DIRECT LOANS				
FY 1979	369	43%	$16,000,000	41%
FY 1980	469	55%	$18,856,000	54%
FY 1981*	455	52%	$18,422,000	52%
GUARANTY LOANS				
FY 1979	295	9%	$22,999,000	6%
FY 1980	287	9%	$21,932,000	5%
FY 1981*	241	8%	$23,588,000	6%
TOTAL LOANS COMBINED				
FY 1979	664	16%	$38,999,000	10%
FY 1980	756	18%	$40,788,000	9%
FY 1981*	696	18%	$42,010,000	9%

* Unofficial.

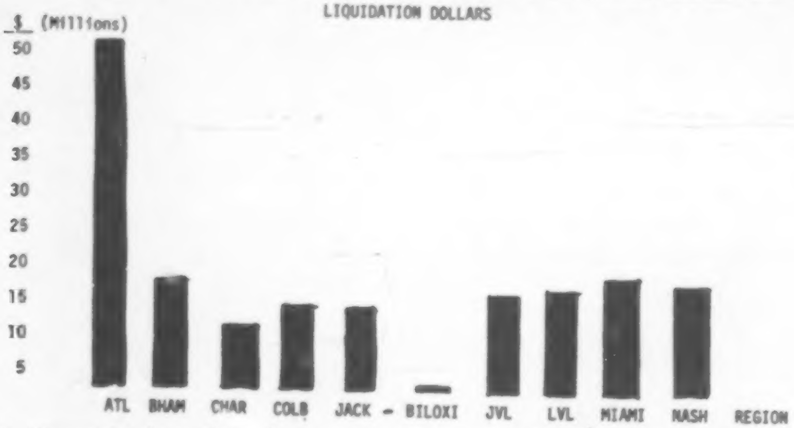
REGION IV

PORTFOLIO CURRENCY RATE



	ATL	BHAM	CHAR	COLB	JACK - BILOXI		JVL	LVL	MIAMI	NASH	REGION
TOTAL '81	73 %	77 %	83 %	79 %	84 %	80 %	79 %	78 %	73 %	86 %	78 %
'80	78 %	86 %	85 %	81 %	85 %	86 %	83 %	76 %	76 %	89 %	82 %
% CHANGE	-5 %	-9 %	-2 %	-3 %	-1 %	-6 %	-4 %	+2 %	-3 %	-3 %	-4 %

LIQUIDATION DOLLARS



	ATL	BHAM	CHAR	COLB	JACK - BILOXI		JVL	LVL	MIAMI	NASH	REGION
TOTAL '81	51.7	18.0	11.1	14.8	14.4	4.3	16.1	17.3	19.0	18.0	185.0
'80	30.5	12.8	6.8	11.3	6.9	4.1	11.7	16.3	14.8	12.3	127.9
% CHANGE	+70 %	+41 %	+63 %	+31 %	+109 %	+ 5 %	+38 %	+6 %	+28 %	+46 %	+ 45 %

	(IN THOUSANDS)				NUMBER OF SMALL BUSINESS AWARDED SUBCONTRACTS		
FY [illegible]	TOTAL DOLLARS	SB	SDB	W/O	SB	SDB	W/O
1ST QUART[illegible]							
E-Systems (Memcor) Tampa	2,687	1469	14	0	2332	12	0
E-Systems (ECI) St. Pete	3665	2687	33	16	2721	25	10
Honeywell-Tampa	3740	1391	34	0	807	20	0
Honeywell (Avionics) - St. Pete	10,509	7036	132	0	11,158	147	0
Sperry	5353	3753	48	0	2850	103	0
Martin Marietta Aerospace	55,407	22,591	725	140	9742	130	25
G. E. - St. Pete	4698	2347	216	18	1677	78	7
	86,059	41,274	1,202	174	31,287	515	42
1ST QUARTER							
McDonnell Douglas	2,089	1818	15	0	725	10	0
Harris Gov't	15,366	9568	126	46	12,135	610	10
G. E.	3,520	1397	97	0	910	18	0
Pan AM	1,230	677	9	8	636	46	5
Pratt & Whitney	20,543	14,990	720	0	3333	235	0
	42,748	28,450	967	54	17,739	919	15
1ST QUARTER							
Teledyne Brown	1869	902	210	5	1275	41	1
Hayes	3426	2566	45	1	2462	251	1
PAN AM, MS	4956	3352	1007	12	2501	51	1
E.I. Dupont	52,923	17,461	684	10	8915	270	11
SCI	3535	1366	96	0	3125	1	0
Ingalls	54,388	21,218	117	0	5483	77	0
Lockheed, GA	44,088	14,078	606	0	9269	143	0
	165,185	60,943	2765	28	33,030	834	14
1ST QUARTER							
Martin Marietta Aluminum	2,906	2272	14	3	670	18	2
AVCO	13,250	685	51	0	456	24	0
Raytheon	9718	5282	211	7	2808	143	35
Bolston	9253	5222	15	5	939	23	18
Western Electric	15,043	3939	218	12	4887	60	22
Union Carbide	84,402	38,097	3042	673	22,630	2037	1082
	134,572	55,497	3551	700	32,390	2305	1159

	(IN THOUSANDS)				NUMBER OF SMALL BUSINESS AWARDED SUBCONTRACTS		
FY'81	TOTAL DOLLARS	SB	SDB	W/O	SB	SDB	W/O
2ND QUARTER							
E-Systems (Memcor) Tampa	5221	3930	16	4	2906	15	2
E-Systems (CMD) St. Pete	2925	2125	21	205	358	10	40
E-Systems (ECI) St. Pete	4812	3696	98	23	3271	90	10
G. E. St. Pete	7381	3139	476	33	1587	283	18
Honeywell Tampa	14,156	7660	36	0	2017	10	0
Honeywell (Avionics) St. Pete	11,868	7577	113	0	10,627	150	0
Sperry	6,608	4443	67	0	3211	49	0
Martin Marietta Aerospace	71,412	28,807	927	223	9917	330	79
	124,374	61,377	1754		33,894	937	149
2ND QUARTER							
McDonnell Douglas	1,336	1079	5	0	690	10	0
Hanes Gov't	19,065	1,649	138	377	15,008	20	8
G. E.	3525	2110	110	0	610	10	0
Pan AM	2656	1579	50	0	612	12	0
Pratt Whitney	25,643	9393	839	184	2506	262	50
	53,561	25,810	1142	561	19,426	314	58
2ND QUARTER							
Teledyne Brown	1898	1166	288	1	1385	12	1
Hayes	6568	4000	187	7	2042	53	1
Pan AM, MS	5223	3497	726	0	2601	49	0
E.I. Dupont	36,752	18,561	1527	0	8406	52	0
SCI	5551	3041	19	0	1825	4	0
Lockheed, GA	133,616	11,690	560	0	10,745	62	0
Ingalls	47,717	22,843	359	0	4873	51	0
	237,325	64,798	3666	8	31,877	283	4
2ND QUARTER							
Martin Marietta Alum.	2782	2016	40	58	674	17	22
AVCO	2178	572	11	0	591	5	0
Raytheon	5274	3820	51	7	1818	101	28
Holston	3084	1931	12	11	947	16	27
Western Electric	43,854	12,912	214	8	9009	171	64
Union Carbide	92,578	28,169	2973	814	23045	2227	1570
	149,750	49,420	3301	898	36,084	2537	1711

		(IN THOUSANDS)			NUMBER OF SMALL BUSINESS AWARDED SUBCONTRACTS		
FY'81	TOTAL DOLLARS	SB	SDB	W/O	SB	SDB	WO
3RD QUARTER							
E- Systems (Memcor) Tampa	7,675	4,133	295	0	2750	210	0
E-Systems (ECI) - St. Pete	3,932	2,518	34	91	2682	36	3
E-Systems (Comm. Mfg.) St. Pete	8,340	5875	440	0	964	78	0
G. E. - St. Pete	6764	4211	122	66	1816	58	30
Honeywell "Avionics"	10,177	6498	126	0	11,096	213	0
Sperry	5629	4079	78	30	2795	55	20
Honeywell "Tampa"	6034	2906	3	0	1949	10	0
Martin Marietta (Aerospace)	95,299	30,131	1522	332	10,425	555	122
	143,850	60,351	2620	519	34,477	1215	175
3RD QUARTER							
Pan Am - Fla	1,958	958	17	10	826	86	10
Harris Gov't	63,193	27,498	278	78	26,572	25	8
G. E. Daytona	3,909	1,728	40	4	800	15	8
Pratt & Whitney	9,654	4,466	474	682	2125	106	148
McDonnell Douglas	1,906	1,671	51	0	926	11	0
	80,620	36,321	860	774	31,249	243	174
3RD QUARTER							
Pan Am, MS	1,616	1342	302	0	2400	4	0
Ingalls	94,611	18329	216	0	4745	42	0
Hayes	2,157	1573	26	4	1712	25	9
Lockheed, GA	38,561	13490	490	0	9296	53	0
Teledyne Brown	2795	1444	149	1	1236	32	1
BCI	4879	2700	4	0	3109	5	0
E.I. Dupont	52,399	26,499	1550	461	9155	68	10
	212,018	65,377	2737	466	31,653	229	20
3RD QUARTER							
Raytheon	3,099	2273	0	0	2209	0	0
Holston	1242	647	2	10	1006	7	49
Western Electric	21,135	7082	54	28	6425	157	28
Union Carbide	73,636	33,214	3155	1488	24,468	2,769	1836
AVCO	4130	2253	190	0	960	88	0
Martin Marietta Alum.	4969	2079	42	17	823	20	24
	108,211	47,548	3443	1543	35,891	3,041	2937

FY'81	(IN THOUSANDS) TOTAL DOLLARS	SB	SDB	W/O	NUMBER OF SMALL BUSINESS AWARDED SUBCONTRACTS SB	SDB	W/O
4TH QUARTER							
Neutron Devices	10,010	4,603	310	58	1930	41	20
E-Systems	1,915	924	26	11	431	12	5
Honeywell	2,575	1,744	74	0	2,134	93	0
Sperry	5,226	4,145	7	1	2470	45	3
Honeywell "Avionics"	15,828	9,014	170	0	1080	270	0
Martin Marietta "Aerospace"	51,095	18,178	988	492	7582	375	210
	86,649	38,608	1575	562	15,627	836	238
4TH QUARTER							
General Electric	2,772	1,776	6	5	629	10	3
Pratt & Whitney	15,625	6,974	249	280	2276	793	2
Pan Am	1,299	1,168	20	23	889	80	6
McDonnell-Douglas	7,650	4,589	104	24	1006	71	10
Harris Gov't	30,688	14,808	364	309	3127	20	8
	58,034	29,315	743	641	7927	974	47
4TH QUARTER							
Ingalls	97,899	24,617	373	0	4423	58	0
Teledyne Brown	4,653	2,544	150	37	1991	21	3
Pan Am	1,327	762	14	0	1798	86	0
Hayes	5,092	2,152	15	24	2160	23	8
Lockheed, GA	40,006	13,847	419	0	8305	218	0
E.I. Dupont	46,549	24,777	1495	1058	9859	70	20
SCI, Inc.	3,921	1,624	10	0	1824	6	0
	199,447	70,323	2476	1119	30,360	482	31
4TH QUARTER							
Martin Marietta Alum	2,949	2,266	24	23	749	23	35
Raytheon	7,737	6,352	288	2	1581	73	7
Holston	3,028	2,325	602	7	903	8	35
Western Electric	17,242	10,888	22	4	7311	114	39
AVCO	2,444	1299	68	0	740	24	0
Union Carbide	91,442	50,769	2570	1404	22,926	192	1747
	124,842	64,100	3574	1440	34,210	434	1863

Total dollars Subcontracted during FY '81	$2,007,245,000
Total dollars to Small Business	799,512,000
Total dollars to Small Disadvantaged Business	36,376,000
Total dollars to Women-owned	9,975,000
Percentage to Small Business	39.83%
Percentage to Small Disadvantaged Business	1.81%
Percentage to Women-owned	.5%
Number of Small Business Awarded Subcontracts	457,121
Number of Small Disadvantaged Business Awarded Subcontracts	16,098
Number of Women-owned Awarded Subcontracts	7,637

FY '80 - 25 PRIMES REPORTING

Total Dollars Subcontracted	$1,629,856,000
Total to Small Business	$ 710,019,000
Percentage to Small Business	43.56%

FY '81 - 25 PRIMES REPORTING

Total Dollars Subcontracted	$2,007,245,000
Total Dollars to Small Business	799,512,000
Total Dollars to Small Disadvantaged Business	36,376,000
Total Dollars to Women-owned Business	9,975,000
Percentage to Small Business	39.83%
Percentage to Small Disadvantaged Business	1.81%
Percentage to Women-owned Business	.5%
Number of Small Business Awarded Subcontracts	457,121
Number of Small Disadvantaged Business Awarded Subcontracts	16,098
Number of Women-owned Business Awarded Subcontracts	7,637

Mr. MITCHELL. Thank you very much. That is certainly one of the most comprehensive statements that we have heard in our hearings around the country, very detailed, and very comprehensive.

Mr. WIDEMIRE. I am blessed with a good staff, sir.

Mr. MITCHELL. Let me just ask you a quick question. I have several, but let me ask you a question on the very end where you talk about a number of these firms, the 24 prime contractors have volunteered for SBA to review their entire subcontract programs to small business. Does that mean subcontract programs separate? You may have your staff join you if you care to.

Does that mean that these are subcontractors that are not covered under Public Law 95-507? Does that mean subcontracting in the private sector?

Mr. WIDEMIRE. Mr. Chairman, if I may defer to Mr. Latimer on that. He is our Assistant Regional Administrator for procurement matters.

Mr. LATIMER. Prior to Public Law 95-507 we had a volunteer program where SBA solicited the help of prime contractors in support of small business. Public Law 95-507 made it mandatory that we review contracts. As we get notification from the contracting officers, we do review those contracts. There are other contracts with a prime that we do not know they have simply because we are not notified or somehow it slips through the mill and we are not aware that the contract exists.

Mr. MITCHELL. These are Government contracts?

Mr. LATIMER. These are Government contracts. We are not being notified.

Mr. MITCHELL. With the Federal Government?

Mr. LATIMER. With the Federal Government, right. These companies have volunteered to let us review every contract they have. Otherwise we would only know of the one contract we were in there to review by virtue of notification.

Mr. MITCHELL. It's very fine they have done that. I am disturbed there would be this kind of slip through. There is just no justification for your not being notified about each contract. That is a part of Public Law 95-507.

Mr. LATIMER. I agree.

Mr. MITCHELL. About how many such contracts are you aware of that have slipped through?

Mr. LATIMER. We found about 10 contracts at Lockheed alone that we were not aware of prior to going in. I am sure there are a lot of companies that have contracts we don't know about. We are only aware of the contract through independent review.

Mr. MITCHELL. Where is the responsibility to be placed on this failure to notify?

Mr. LATIMER. With the procuring agencies, the Government procuring agencies.

Mr. MITCHELL. In other words, Interior, GSA might not let you know——

Mr. LATIMER. DOD.

Mr. MITCHELL. That is certainly something we need to check up on. There could be literally millions of dollars that could be available to small and minority businesses that are not being made available simply because the information isn't passed on to you. I commend you for the volunteer aspect of these prime contractors, but I don't think that quite makes up for a deficiency in the system. That is a deficiency.

Gentlemen, I will put the questions to both of you, if I may. What is your thinking about the new graduation program from the 8(a)? Let me indicate to you that during testimony in Washington a businessman from California testified before our subcommittee.

Newt, he was very kind to announce that he was a conservative. He didn't believe in any Federal Government programs, but he did go on to point out the absolute folly of forced graduation of firms from the 8(a) program. He went on to indicate if this takes place, then he predicts that over 50 percent of these firms will fail after the Government has invested all of this money bringing them to the point that they are at.

What is your comment on the new graduation program?

Mr. **Widemire**. That would be my personal comment, Mr. Chairman, if I may.

Mr. **Mitchell**. Yes.

Mr. **Widemire**. If you would consider it in that light.

Mr. **Mitchell**. Certainly. This is personal. The record will indicate that.

Mr. **Widemire**. There is a need, and I believe Congressman Gingrich sort of referred to it earlier. There are 14 million small businesses out there. I have forgotten how many of those are minority, but there are a considerable number of those that are minority. We have—what?—about 2,000 nationally, 2,100 8(a) contractors.

It is imperative in a sense that there be some graduation of those who have had an opportunity to develop and have either developed or have not developed under the assistance, the multifaceted assistance of 8(a) in order to create room in order to bring in additional people and give them the same opportunity to prosper. This is my personal view, Mr. Chairman.

Some firms have done very well under our 8(a) program in this region, done very well. We are very proud of them. We would like the opportunity to bring some more in and give them that same opportunity.

Mr. **Mitchell**. Could I pursue that a little bit more? I am in agreement with you. Of course, there has to be some kind of graduation. You can't leave firms doing business with the Government under the 8(a) program ad infinitum, but my question, more specifically, is the length of time that has been established for graduation, it is in that area. That is a forced graduation, beyond the phaseout period of 1 year, there is no other alternative.

Is that a sufficient length of time to insure that the firm that is going through the 8(a) program successfully is prepared and can compete in the private sector?

Mr. **Widemire**. Mr. Chairman, my personal experience in business, and my personal experience prior to coming with SBA and watching other small companies become established and developed is that the typical company is either going to be successful in the 3-year time or maybe 4-year timeframe, in a 2- to 4-year timeframe, or it is not ever going to be. That is my personal experience.

I have seen it in many, many companies. My own little company, the third year before we became really successful. The first year we lost money, second year we did well to break even, the third year we became successful and have remained successful. This is typical of the smaller businesses with which we are dealing.

Beyond that, sir, you get into questions of management. If management hasn't made it successful in that timeframe, the likelihood is that they are going to be.

Mr. **Mitchell**. Even taking into account such factors as perhaps the differentials in practices of lending institutions, differentials in terms of access to capital that would affect an 8(a) firm as opposed to a non-8(a) firm, you would still adhere to that posture?

Mr. **Widemire**. Part of the 8(a) program is providing some of the facilities to overcome those lacks in the marketplace.

Mr. **Mitchell**. But they haven't?

Mr. **Widemire**. In many instances. We have provided capital, business development funds. It has to be in the nature of capital.

Mr. **Mitchell**. Under the SBA program?

Mr. **Widemire**. Yes, sir.

Mr. **Mitchell**. I am saying a firm comes out of the 8(a) program, it is forced to graduate. Then it has to depend upon its capital, its access to capital in the private sector, does it not?

Mr. **Widemire**. Of course it is our objective and hope that the opportunity we are giving these 8(a) contractors, that they will have a running start and will be a profitable company in their category at that time. That is our hope.

Mr. **Mitchell**. I won't pursue it. But your hope flies right in the face of volumes of testimony that we have received throughout the years, that it is just exceedingly difficult for an 8(a) firm to have the same access in the private sector to everything that he needs.

You talked about the disaster loan program, which is very near and dear to your heart evidently.

Mr. **Widemire**. Because it is so consumptive to us.

Mr. **Mitchell**. Certainly because you and your staff spend a lot of time on it. We heard time and time again the criticisms about the disaster loan program by Members of Congress, that it is abused, that the large agribusinesses benefit from it when they really should not.

We have heard testimony to the effect that there is padding which goes on in terms of the disaster itself. "Not only were my crops destroyed but my four Van Gogh paintings I purchased 10 years ago were destroyed." Just reams of criticisms about abuse in this program. What is your response to those criticisms?

Mr. **Widemire**. There does appear to have been considerable of that. I believe there was a hearing back before I came on board, maybe in August or September, that covered many aspects of that. One of the primary roles of our additional 99 disaster loan servicing personnel—which incidentally wasn't 99—it was about 60 some-odd—because we had 30 on board and they got shifted from one category to another.

Mr. **Mitchell**. That is shortchanged. You need them over in the other category.

Mr. **Widemire**. Right.

One of their primary functions is to try to ferret out what some people refer to as double-dippers, double users of benefits of the Farmers Home Administration benefits, ASCS benefits, and our benefits. We do our best to re-collect those apparent abuses. Some of them were quite abusive, some of them were only apparent abuses that didn't turn out to really be abuses in certain instances.

Mr. MITCHELL. I certainly believe you. That is, unfortunately, the problem with many of these critics. The criticisms hit the press and then when the real truth comes out, there is no notification that there was no abuse.

Mr. WIDEMIRE. That is correct.

Mr. MITCHELL. I see the mayor is here.

Mr. WIDEMIRE. Half of those numbers turn out to be nonabusive.

Mr. MITCHELL. Our new mayor is here. That means instead of the other 10 questions, I will cut it down to 5 for you. I don't want to impose on the mayor's time.

Mr. WIDEMIRE. Thank you, Mr. Mayor. [Laughter.]

Mr. MITCHELL. Some "enlightened" person in Government—enlightened in quotes—is toying around with the idea of making small businesses pay something for the management assistance given to them. What is your reaction to that?

Mr. WIDEMIRE. You are speaking of the management assistance programs that SBA itself——

Mr. MITCHELL. Right. Someone is toying around with the idea, in one of the deep chasms in Washington, of saying you must pay something for it. They aren't going to give anything away free. We don't care if you are that little-bitty business Newt Gingrich talked about. If you come in and ask for management assistance then you have to pay. If you are better off, you will pay more. What is your reaction?

Mr. WIDEMIRE. I haven't thought about that one, Mr. Chairman. I would not be in favor of charging for the basic services. For instance, if we had some extra services, where we bring in some hired help, maybe some sort of modest charge to cover out-of-pocket costs. Some very modest arrangement like that might be reasonably satisfactory. But for the basic services of our SBA personnel, I would not look with favor on that right off the bat.

Mr. MITCHELL. Well, I certainly share your feeling. I think the people who come to us for help just simply in most instances cannot afford to pay.

Mr. WIDEMIRE. May I add to that for just a moment? What we are trying to do is to examine as to how we can get on the front end of the management assistance delivery as opposed to the rear end. What we find so often is the small business person who is calling on us for management assistance is too late. They are too down in the hole.

If we can reverse that process and get it up on the front end, particularly with the borrowers and assistance needed that Congressman Gingrich referred to, in that area if we could get up on the front end, the truly small, as he says the "baby businesses," if we could get up to help on the front end of that, I think our delivery of services and assistance would be magnified considerably.

Mr. MITCHELL. I agree. Let me congratulate you for the work done on page 9 under your prime contracts and your general, almost doubling of moneys to small businesses and under the set-aside program.

Let me congratulate you on the breakout procurement activity. That is a fascinating development, one that I would like to see at least experimented with in other sections of the country. I don't know whether it is being done or not. It is certainly an efficacious way of facilitating small business activity.

Mr. **Widemire**. Thank you very much.

Mr. **Mitchell**. Page 8 of your testimony was the good part. Page 8 is not the bad part. I just have a question. I am concerned as I look at financial assistance that you have shown a steady increase from 1979 in minority loan activity of about $2 million a year. Right?

Mr. **Widemire**. Yes, sir. Approximately 5 percent.

Mr. **Mitchell**. Certainly you are moving in the right direction, but that seems to me to be awfully slow progress.

Mr. **Widemire**. You have to put that within the framework of total direct lending reducing guarantee, Mr. Chairman. That represents a significant stride, considering that the total is reducing, that that portion to minority is increasing is good progress, sir.

Mr. **Mitchell**. Those are your words, "good progress."

Mr. **Widemire**. It seems to me, sir.

Mr. **Mitchell**. One last question. That is on page 7. I have to explain why we raise this question. I have gone bananas sometimes in Washington over the last 10 years when we have had MBDA come in to testify. It was the minority business development assistance program. Then the next day SBA would come in and say we also have helped 38,000 businesses. Then somebody else would come in and say we have helped 38,000. When we started checking, they were dealing with the same populations.

My question is with reference to the management assistance, one cadre of people provided management counseling to 23,113 firms, bottom of page 7. Then the small business development centers counseled another 6,132. Your SBA and others provided management training to 38,000.

How much duplication is there, do you know? How do you separate it out so that you know that guy is not counted under your program and under the small business development centers and under something else?

Mr. **Widemire**. Under the small business development centers, they are not duplicates. There could possibly be duplicates with MBDA. That is a Department of Commerce program?

Mr. **Mitchell**. Yes.

Mr. **Widemire**. There could be possible duplication there. Some duplication could have been jointly sponsored conferences that we both could have counted. There could be some duplication there.

Mr. **Mitchell**. There has to be some way to avoid that. I think this is awfully misleading. It is tough to avoid.

Mr. **Widemire**. That would be relatively modest.

Mr. **Mitchell**. I go to the conferences around the country as often as I can. I see the same faces. There has to be some way of presenting figures which are not potentially misleading.

Mr. **Widemire**. Let me ask my associate if he has any comments. Could he add to that?

Mr. **Scoggins**. I don't have access to the MBDA figures.

Mr. **Widemire**. I might add this, Mr. Chairman: It would not surprise me that many enterprising—particularly minority enterprising—people would be seeking assistance from both agencies.

Mr. **Mitchell**. That doesn't surprise me. I think a good guy is going to be out shopping around every place that he possibly can. I do hold, however, that it is misleading; it can be very misleading—when the same person goes to five different conferences and is counted separately each time and you get the idea that you are doing a lot more for a lot more people than you really are. I am not at all sure that the conferences themselves, just the attendance at a conference, should be counted.

Mr. **Widemire**. Seminars, learning process centers, seminars, SCORE contacts, they may be counted by SCORE, by our own personnel staff, and there may be duplicate countings there, of the same person, but that is productive, in a sense. It is productive in that he is getting that much aid and making use of it. In that sense that is very productive.

Mr. **Mitchell**. I am not going to tautologize this discussion, but I don't think it is very productive when the same businessman goes to five different seminars, all of which are conducted on the basis of general management assistance. You are reinventing the wheel five times. I think it is productive when he sits down on a one-on-one basis with someone. Say now here, this is what you need to do, here is what you can do to strengthen this, here is what you can eliminate.

Well, thank you very much again. As I say, it was very comprehensive testimony. We appreciate you and your staff being here.

Mr. **Widemire**. Thank you, Mr. Chairman. It was a pleasure. We hope you will hold one of your other four hearings with us.

Mr. **Mitchell**. I am just delighted that Mayor, Ambassador, Congressman, Pastor, that Mayor Young is here.

Andy, it is a pleasure to see you, sir.

May I shake your hand?

TESTIMONY OF HON. ANDREW YOUNG, MAYOR, CITY OF ATLANTA, GA., ACCOMPANIED BY DAVE MILLER, DIRECTOR, OFFICE OF CONTRACT COMPLIANCE

Mayor **Young**. May I take this opportunity to bring greetings to you from the city of Atlanta. I thank you for braving our cold weather and promise you that if you come back, we will be doing better. We are glad to have you looking into our small business situation, because I think there is nothing that is more critical as I begin this administration than the possibility of generating new job opportunities.

I think we have just about accepted the fact that most of the job opportunities that are to be generated in this city will not be generated by big business at this point but by a wide variety of small business opportunities. I think Mayor Jackson laid a very good foundation in providing opportunities for small business and particularly minority firms to have the beginning of a fair share of city procurement and of opportunities to participate in various Federal projects.

Most of those opportunities are running out, however, and we find ourselves with high interest rates, with even higher unemployment, and small business basically struggling to find ways to stay alive.

I have been impressed with the concern that the total community has—even to the point of one of our churches as a local congregation deciding that it was going to raise $100,000 to assist small businesses in the neighborhood of the church.

I would certainly like to see that sort of thing encouraged, but I think encouraged in isolation would not be nearly as helpful as it would be to encourage investment in neighborhoods by private groups under a broad framework that might come out of your committee, Mr. Chairman.

We also have an enormous infusion of capital proposed by these IRA accounts. I am not sure what kind of encouragement the banks are going to have in making some of this money available for small business, particularly minority business, but I am not here to testify. I am really just learning my way to the restroom.

I found my way to the State capitol, and this is just my second week. We have had to face this snowstorm. So I really am not prepared to testify on behalf of the city, but Mr. Miller, who is the director of our office of contract compliance, does have testimony and will speak in our behalf and answer any questions you might have.

Mr. MITCHELL. Mr. Mayor, I certainly appreciate your coming here. We have Mr. Miller's testimony. We will hear from him next. The climate here is quite salubrious compared to the Baltimore-Washington area. The precipitation is minuscule in this area compared to the Baltimore-Washington area or farther up the coast. Please make no apologies. It is a vast improvement over what we left in the Baltimore-Washington area.

I made a note about your mentioning the possible use of IRA accounts. That is something we need to pursue. Congressman Gingrich was with us. He had to go to a meeting with the Atlanta Journal editorial board at 10:30. He knew you were coming. He extends his best regards. Congressman Hatcher, unfortunately, is having water problems in his hotel and apparently has not been able to go through his morning ablutions. As soon as those little problems are cleared up, I am certain that he will be here. I am certain he would also extend his best wishes for your continued success.

Might I just say, Mr. Mayor, as chairman of the Committee on Small Business, if you think I can be helpful to you, please do not hesitate to call at any time. You will get a very high priority. A little below Baltimore and one or two other cities, but a high priority.

Mayor YOUNG. Thank you very much.

Mr. MITCHELL. Thanks, Andy, a real pleasure.

Mr. Miller.

Mr. MILLER. I think the concern we have had in the city of Atlanta over the last 6, 7, 8, years is the creation of opportunities must exist within a governmental framework. The Government must take the opportunities and then indeed bring forth opportunities so business people can go into business. That is the first key.

I think the second major concern of ours is that the problems of access to those opportunities, where we find that opportunities exist, we also find some business people come forth and take advantage of those. We find largely those business people are the same. We must address the problems of access. Access being insurance, financing, bonding, all things critical and key to the development and growth of any business.

Mind you, those things are key to all business, but they affect minority businesses much more greatly than other businesses, primarily small businesses.

We want to challenge the committee to look for those uniform regulations or practices that a committee can have influence on such as the IRA, having some of those moneys earmarked for use in the inner cities where primarily our financial institutions are located.

Other earmarking is what I understand under the SBA program that all banks do not participate in the lending arrangement. I think it should be a condition of a bank participating in any Federally assisted programs, loan guarantees, IRA accounts that they also participate in the SBA loan arrangement.

I found minority owning business people who traditionally have banked with one bank and developed a friendship among the banking offices there are often referred to other banks to get SBA assistance. That cuts the consistency and the working arrangement between "Do I know you?" as opposed to not knowing you, working in the cold, you are not kept there in that banks are having to send their customers to other banks participating in the loan guarantees program.

Those are the kind of things we want to see changed. Federal regulations that make it mandatory for all banks who take advantage of Federal dollars or work with the Federal Reserve Board have to consistently apply themselves and use other regulations within the Federal Government as well. I think that is a key consideration, consistent, uniform.

Mr. MITCHELL. That is a very key recommendation. The lending institutions should not be able to have it both ways.

Mr. MILLER. Exactly.

Mr. MITCHELL. They shouldn't be allowed to benefit through legislation and programs that are beneficial to lending institutions and then shirk off any responsibility when it comes to the loan program for small and minority businesses.

Mr. MILLER. There is also consistency and key in other industries as well. While the cities can regulate certain aspects of business opportunities and growth within its borders, we find it very difficult, sometimes impossible to regulate those things outside of our concern. Specifically insurance and the bonds in this city. It is a closed market. Minority firms and small businesses find it difficult to secure those bonds.

We understand those insurance companies are getting dollars from the Federal Government. What we are looking for from our vantage point is that we use additional minority businesses, additional small businesses, and additional women-owned businesses for those people to be given the support at other agencies that limit their growth and their ability to participate with us.

You have all heard, probably, about our success at the airport in terms of minority businesses. I think that comes from a commitment to make things work. The same assurances we placed on getting concrete poured properly, getting a building erected properly is the same assistance we place on the use of minority businesses. We want to be assured they participated. We didn't leave it to chance. Our bonding requirements, our insurance requirements, our payment schedules were restrictive and prohibitive. We changed those things. That was our commitment to make it conducive for small business and minority business to participate.

What I am suggesting here is that whatever the Federal payment schedule, Federal requirements, Federal requirements for contractors, and the use by various agencies need to be reviewed. Where they were not applicable or too stringent, as we said the punishment was too strong for the crime, we think it should be changed. A lot can be done by mandating certain things be changed.

In September we had an opportunity to talk about the 8(a) graduated program. The gentlemen from SBA are more knowledgeable than we are about this program, but as I understand what is happening is, that the Federal Government is creating or identifying businesses who can supply them with goods or services or get a job done for them.

We also understand these are not jobs being created by the Federal Government just for that sake. They are basic needs of the Government. It would seem a little inconsistent for us in terms of interrupting what is happening if these services or jobs can be done. We believe it behooves the Federal Government to increase the numbers for as long as they can stay there to provide the services for the Federal Government. These are not questions being created. This is opportunity the Government has for anybody to secure. So why force a person out in 5 or 10 or 20 years? As long as the services are needed by the Government, there should be intrepreneurs sought after to take advantage of the program to get your best competitive prices.

By way of example, some things we have done. The Federal Aviation Administration here paid us a nice comment back in 1978 when they reviewed us in terms of its DOT program, in terms of minority business participation. They found out the 27 largest airports in this country, Atlanta generates 27 percent of major airports.

You talk about major airports like Chicago, Baltimore, Washington, D.C. At that point in 1978, $56 million went to minority business. Fifty-three million dollars went from Atlanta. We think we are still way far ahead. We probably will stay that way.

I think the airport, because it is glamorous, does not tell our real story. Even in the less glamorous projects, like the EPA projects, minority businesses are participating at a rate of 33⅓ percent. Engineering design and construction is about 45 percent. We see the ability here of the businesses to perform for us as great.

We have to provide an opportunity for them to do so and access for that opportunity, that is, rules and regulations consistent with creating opportunity. We have to make sure the businesses survive.

Thank you.

[Mr. Miller's prepared statement follows:]

PREPARED STATEMENT OF DAVE MILLER, DIRECTOR, OFFICE OF CONTRACT COMPLIANCE, ATLANTA, GA.

Welcome to Atlanta. Our history is diverse and strong in support of Federal efforts and indeed all efforts to improve the economic stability and growth of small and minority business. If Atlanta is not the genesis in this regard, we are certainly one of the first franchises. Atlanta has been called the Mecca for Blacks and other minorities. She carries the title proudly and continues to make strides to retain the title and share with others the need and desire to have each village, hamlet, city, state, in our great nation a Mecca for all its people. This is the goal, this is the challenge, this is the work that is left for us to do.

One major step, of many to be taken, is to hold important hearings such as this. While we view Washington in many different ways, we see through these congressional hearings a serious governmental concern of the citizens of this country. In this manner, government and the lawmaking process can and does come to the people.

I appreciate this opportunity to testify before you today (on behalf of Mayor Andrew Young and the Atlanta city council) on the role local and state government must play in furthering the efforts of small and minority business and in assisting the federal government to foster their development. We believe our role to be clear yet complex, comprehensive and characteristic of those things necessary for the free enterprise system to work. Therefore, simply stated, the role of City, State, and Federal Government must be the creation of markets, thus creating opportunities.

Without market opportunities, there is no impetus for any firm, small or large, minority, or non-minority to venture into business. Therefore, our chief concern becomes creating legislation, developing appropriation packages that provide for the maximum opportunity and to the maximum extent possible, for the development of opportunities—market.

The past has shown us that when business opportunities arise new businesses develop to take advantage of them. This is the basic fashion in which the free enterprise system works. However, the past also has shown us virtually a systematic exclusion of businesses owned by blacks and other minorities. Hence, it is not enough to create or provide for market opportunities. This is the critical and delicate challenge to the role of City, State, and Federal government in helping to create business opportunities. We have seen various catch words, code words, utilized by State, City, and Federal governments and private industry to deny access to opportunities to a major segment of our population. Qualifications, experience, bonding capacity, and finances have been barriers to opportunity. Unfortunately, all too often these barriers have unduly and disproportionally affected Afro-Americans and other minorities. We have heard too many stories of: "How do we get qualified, if no one will give us a chance? "How can I get the experience, if no one will let me do it? "How do I get bonding, if you will not bond me?" "Why won't you make a loan so I can do it?"

Distinguished member of Congress, as you can see, we have two (2) concerns: (1) Equal opportunity so that every person will be allowed to participate in and receive the benefits of the public sector without regard to race, creed, color or national origin; and (2) equal access. In this one, equal access, lie the root causes of the problems.

Many times the makeup of equal access is beyond the reach and authority of State government and, almost entirely, City government. For example, we do not regulate the insurance industry, or the banking and financing community. Neither can we create uniform business and industry regulations which transcend city limits. In the relatively few areas where we have municipal regulations we become an island of help in a otherwise sea of crushed hopes and aspirations. The Cities can and will continue to support the Federal government in ensuring that equal opportunity is the law of the land, but the Federal government must take the lead in providing consistent, statutory provisions to eliminate discriminatory practices in the area of equal access.

By way of example, I want to describe for you what we have found in the City of Atlanta. In 1973, the City of Atlanta had total contract opportunities in excess of

$30 million, of which less than .13 percent was awarded to Minority Firms. In the first year of the Jackson Administration, we set out to change this. It was obvious to us that there was something dramatically wrong when business opportunities of the magnitude we had to offer were being shared with minority firms in the absurdly low percentage of less that 1/10th of 1 percent. In the ensuing years we have developed methods and procedures seeking to remove discriminatory practices from access to opportunity in the City of Atlanta, and we have succeeded.

How have we done this? We have devised payment schedules for contractors to facilitate the cash flow of both prime and subcontractors. We have devised for most construction contractors fifteen (15) day payment periods, thus eliminating or otherwise reducing the impact of cash flow and of the inability to obtain outside financing. We have, where appropriate, reduced or waived bonding for prime and subcontractors based on a review of the ability of the company so as to minimize or otherwise eliminate the effects of discriminatory practices in the bonding industry.

We also have agreed to reimburse the prime contractor and subcontractor for purchases of materials and equipment within thirty (30) days, therefore eliminating the need for major financing of materials and equipment by the contractor. In addition, we have taken the traditional affirmative steps such as breaking down contracts into smaller work elements, providing technical and management expertise and working with contractors to develop procedures that will allow for smaller firms to participate.

We started this process in 1974 despite the public outcry from many businesses who claimed that our affirmative action plan, and our encouragement of joint ventures would increase costs and delay projects. We have a wonderful testimonial in reverse—the City of Atlanta's Hartsfield International Airport.

By using methods previously discussed, we have built the largest airport terminal in the world as well as many other City projects with unprecedented and unequalled levels of minority businesses participation. Minority businesses also are providing many services for the City of Atlanta such as: external auditors, architect and engineering services to the tune of 33⅓ percent of needed services. In addition, minorities are involved as management consultants and prime contractors in parks, housing, and commercial developments. While many now consider our citywide programs as routine, and as an integral part of doing business in the City of Atlanta, we cut our teeth while building the new terminal at the Atlanta-Hartsfield International Airport.

Let me give you just one (1) of many examples: In a study commissioned by the Federal Aviation Administration in 1978 to review and ascertain the levels of contracting with minority businesses in this Country's twenty-seven (27) major airports, it was found that of the 56.3 million dollars awarded to minority firms in those twenty-seven (27) major airports, 52 million dollars has been awarded to minority firms in Atlanta. Gentlemen, nearly 89 percent of all federal dollars being awarded to minority firms involved in construction projects at those twenty-seven (27) major airports were contracted through the City of Atlanta.

While we are very proud of this fact, we will not rest on our laurels. We must continue to address the need for federal legislation that enforces equal opportunity in the various industries that are limiting equal access to opportunity for minority firms.

Clearly, enough has not been done. We cannot merely develop a 10 percent setaside program, or an 8-A Setaside program without reviewing all the many problems that limit the development, growth and survival of minority businesses. To some extent, these problems are the same problems that were attendant in the past, that is, discrimination by those in the access industry.

In summary, we can not provide specific legislation for you and we all know that magical formulas do not exist. Our country, however, needs comprehensive legislation dealing with the effects of discrimination and ensuring that these practices will not continue between individuals, or in business and industry. You, as members of Congress, have a unique opportunity and a great responsibility to enact such legislation ensuring fair, equitable, non-discriminatory practices which, in the end, will benefit our society as a whole.

Mr. MITCHELL. Thank you. I was anxious to have your testimony as part of the record. It is evidence of the fact that where there is a commitment, it can be done and be done successfully. So far Atlanta has not collapsed because you have utilized minority firms to the maximum that you possibly can.

I feel very comfortable coming into your airport, far more comfortable than I feel going to O'Hare. I think the lesson that we ought to learn from Atlanta is if there is a commitment made at the top—city, State, Federal—and if that commitment is really honored and stuck to, then this will work. Of course, there will be cries of outrage as occurred here, but I don't know of any non-minority firms that went out of business because minority firms were utilized at the airport. I don't think any other majority firms were squeezed out of the picture altogether.

I want to commend you and thank you and the former mayor for that enormous effort that you made and the example that you set for the rest of the country.

You have waved bonding frequently?

Mr. MILLER. Yes.

Mr. MITCHELL. How has that worked out?

Mr. MILLER. On nonessential items, our program is based like this. At the conception of a project, we identify where the potential use for MBEs and small businesses are at that point, before we put one drawing down or one spec together. We know in the areas of brick masonry work, concrete work, those traditional things minority businesses have done, why bond them if they are part of a subcontract project? We ask the prime contractor to develop a program to waive and assist people with bonding.

We prequalify all contractors, which is the key consideration we have here. We review that technical ability, financial ability, their track record and their ability to meet our goals and objectives. Once we are satisfied they can do so, we allow those people to be qualified. We know who we are dealing with from the limited scope.

There are companies that have reshifted it. Let me give you an example of what is happening in the Atlanta area. At the Atlanta Airport, essentially highway construction, runway, flat pavement work, minority firms who participated in contracts did it to the tune of 30 to 40 percent. On similar DOT work in the State, the DOT cannot achieve a goal of 2 percent. We say there has been consistency and commitment. Contractors on the DOT side say we cannot meet the goal. Yet we are exceeding those goals in reaching 30 to 40 percent participation.

Mr. MITCHELL. I think it is good that you prequalify. I think the whole process you use is excellent and get firms with a good track record. However, one of the problems I am consistently confronted with at SBA and various agencies of Government is the firm that looks good but doesn't have a track record.

There's always a tendency to say we don't want you, you are relatively new and you don't have a track record, we can't use you. That seems to me being one way to effectively preclude the growth of minority business.

Mr. MILLER. I think the prequalification mechanism we use allows us to identify how qualified a firm is and where they may be deficient, and gives us the opportunity prior to bid, prior to consideration of award, to identify where we need it or where we can overlook the deficiency.

I think it increases competition, increases growth because they get a fair review very early on.

Mr. **Mitchell**. My last very gentle question for you is, what, if any, has been the nature of the relationship between the Government of the City of Atlanta and your local small business administration?

Mr. **Miller**. Well, it is not as good as we would like for it to be.

Mr. **Mitchell**. On a scale of 1 to 10, where would you rate it?

Mr. **Miller**. Seven and a half.

Mr. **Mitchell**. Why?

Mr. **Miller**. I think because of the changes. This happened in Washington. Some of the changes that have happened here locally.

Mr. **Mitchell**. What sort of changes?

Mr. **Miller**. Changes in personnel sometimes. We do not see SBA consistently as we see a lot of contractors. We call them and send people to them. We appreciate them being in this community. If you all can give them more money and staff, I think they could do a better job for us.

Mr. **Mitchell**. I am a very generous congressman. I would give them everything they need. Congress is made up of 435 representatives. I think the likelihood of any more money coming in this, an election year session of the House of Representatives, is just about nil. What have been the problems you have had with your local SBA, if any?

Mr. **Miller**. Not enough notice in terms of when things were bad on their side of the House. Recently I think in December the SBA ran out of money for those loan guarantees. That caught us off guard. A number of contractors who wanted to bid for us were planning on the SBA. We had to restructure bid dates. That is part of our commitment. We just pushed the bid dates back into January. Had we not had this problem—transfer of information is consistently what it is.

Mr. **Blackistone**. I noticed on the news last night a small business in Eastport suffered a huge fire loss. The ranking Republican on the committee, Congressman McDade, represents a district in the Northeast which has a serious fire loss problem among small businesses. Just last week, in fact, five businesses in a shopping center were burned out. Is that a serious problem in this area?

Mr. **Miller**. I think fires are a problem in all major cities. Destruction of businesses by fire, as a minority business, we are not aware of a major impact of that. Here again, I think the insurance regulations and the insurance industry is where we can take a look at that. I do not think the insurance industry is regulated by the Federal Government.

Mr. **Blackistone**. In what respect?

Mr. **Miller**. I think consistently in insurance policies. The rate the policies are issued, the monetary rate for those things, if they are being restricted by area and locale. Businesses of this type are going to be in the most blighted areas of town. I think if the insurance industry is following the practice that has been alleged that the banking industry follows, I think you have a problem. Specifically, minority business will have a problem securing insurance at favorable rates.

Mr. **Blackistone**. Thank you.

Mr. **Mitchell**. Thank you so very much. Just keep up the good work and redouble the effort. The slogan on my staff that they hear from me all the time is, you can do more and you can do better.

Mr. **Miller**. We certainly think so. We are going to try. Thanks for coming to Atlanta.

Mr. **Mitchell**. Our next witness is Melba Williams, president of the Georgia Small Business Council, whom I had the pleasure of meeting in Washington. We are in session. Thank you for coming back with us.

TESTIMONY OF MELBA WILLIAMS, PRESIDENT, GEORGIA SMALL BUSINESS COUNCIL

Ms. **Williams**. Chairman Mitchell, members of the staff, small business people, I am very happy to be here. I am representing the Georgia Small Business Council. I served as its first president and just recently have gone out of office and am now the chairman of the executive committee.

I appreciate the opportunity to appear before the House Small Business Committee on issues that affect our businesses, our Nation's economy, and the lives of millions of Americans.

The Georgia Small Business Council was created in February 1980 by delegates who had attended the first White House Conference on Small Business. One purpose of our council is to follow through and assist in implementing the 60 goals and 15 priorities adopted by the White House conference. We are also concerned that our State laws and government policies are properly tailored to meet the needs and potentials of small business.

The Georgia Small Business Council represents small business interests both in Washington and at our State capitol. Our membership is comprised of business owners and others interested in small business throughout the State. We are also a part of a nationwide network of small business associations dedicated to keeping small business healthy and growing.

We were asked to give our views on two primary issues: taxation and governmental regulations.

First, with reference to the 1981 tax bill, we appreciate the fact that it contains many provisions that will assist small business: Estate and gift tax reform, research and development investment credits, increase in the number of subchapter S shareholders, small reductions in corporate tax rate for corporations with incomes under $50,000, limited direct expensing, accelerated and simplified depreciation, simplification of inventory accounting, and tax credits for used equipment, among others. However, we also recognize that the original tax bill, as proposed by the administration, did not contain many of these provisions. They were accepted from House and Senate Small Business and House Ways and Means Committee amendments.

There was definitely a big business bias in the tax bill. If 80 percent of the Nation's corporations have incomes of under $50,000, as was stated by Senator Weicker, chairman of the Senate Small Business Committee, in urging corporate tax reduction for this group, it is equally true that small sole proprietorships and partnerships constitute the vast majority of these businesses.

Yet individual tax cuts were not targeted to this group, but toward big business. The immediate cut of 20 percent in the top marginal tax rate and 8 percent in capital gains, as well as the accelerated and simplified depreciation which covers only new equipment, are all big tax breaks for larger businesses and higher-income business persons. The additional $25,000 in used equipment available for investment tax credit is entirely inadequate.

The 1 percent reduction in 1982 and 1 percent in 1984 in corporate tax rates for businesses earning under $50,000 will help some, but does not begin to equal proposals for widening tax brackets and reducing rates that were in the Ways and Means bill. The minimal optional expensing provision of the final tax bill is not adequate.

As one small business president, whose company grosses about $4 million a year, told me recently, "I would buy a mini-computer immediately if the $25,000 direct expensing provision had gone through. As it is, I'll have to wait."

Of course, those who understand and espouse the theory of "supply side economics" as does my own Congressman, look on the tax bill not so much as a tax cut, but as a means of balancing the budget and providing savings for investment capital.

As stated in a recent Athens Banner-Herald article from which I quote, "It has been argued that the Reagan proposal was aimed more at the wealthy than lower and middle income earners," and Congressman Barnard indicated that he backed it for essentially that reason. The Democratic version, he said, was "not geared toward savings and investment but toward consumption. Not toward income producers, but toward those who would probably spend the money rather than invest it."

In other words, to make supply side economics work, these poor rich people will just have to bite the bullet, accept the money, and cry all the way to the bank. It is an unproved theory which, if it works, will cause infinitely more pain in the process for small than big business persons and for low and middle income than higher income individuals.

The Georgia Small Business Council, at a recent meeting, voted to request your support for the following taxation and capital formation provisions:

(1) Direct expensing of up to $25,000 per year for new or used equipment, machinery, and vehicles.

(2) Graduated corporate tax structure with provision for wider brackets and lower rates, similar to that proposed by the House Ways and Means Committee in the 1981 tax bill.

(3) Raise number of stockholders allowed in corporations before they are forced to comply with SEC regulations from 15 to 20 or 25. The present minimum is too low to allow small companies to attract sufficient numbers of small investors to meet capital formation needs. Cost of "going public" is $50,000 to $100,000, well above the means of most small businesses.

(4) Exempt from income tax the first $25,000 of profit for a small business which retains the money in the business for capital needs. I know some of the provisions have asked for tax exemption for the first $25,000. We are not asking for that unless the company would be willing to invest it in its capital needs.

The biggest problem facing many of us in small business today is the related one of high interest rates. A story in the Atlanta Constitution of August 11, 1981, states that a very successful 50-year-old catering and restaurant firm, Cloudt's, is closing soon. It has now closed; its owners attributed his problems to "too much borrowed money" and the high interest rates.

My husband, a sociologist, points out that the loss of a business, respected and depended upon in its community for 50 years, also constitutes a tear in the social fabric of that community. He insisted I put this in for you, Mr. Chairman.

Mr. MITCHELL. I am glad he did.

Ms. WILLIAMS. Real estate and automobile dealers are suffering greatly from these high interest rates, and the resulting sales reductions are, as always, having a ripple effect throughout the economy.

This was written for presentation in November. It is more true today than it was then. It has resulted in the high unemployment rates and the decreased production we are experiencing today. Although the all-savers certificate approved in the tax bill seems to be helping the ailing savings and loan associations, it is not according to a recent survey reaching the higher bracket taxpayers it was expected to attract. The majority of investors thus far have been in the middle and lower income brackets. These are the same sources savings and loan associations have always depended upon. Many of the investors merely transferred their money from CD's to all-savers certificates. Higher income people prefer liquidity and investments to savings interest. If we are really serious about increasing bank and savings and loan association funds for use in lower-interest loans for homes, automobiles, and small business needs, then we must make it profitable for middle and lower-income people to save.

The all-savers certificate does not do this, and its use will be limited as soon as this is fully realized. I would like to add here that the expansion of IRA's in the long run increase this savings potential more than the all-savers certificates. I would like to suggest that tax-free savings for homeownership or higher education might do even more.

I certainly agree with the statement that the mayor made about IRA's and also about—I would like to emphasize—the part about the bonding requirements. It is a very vexing problem for minority- and women-owned businesses to get bonding, particularly when they don't have the track record behind them.

As an example of this, my own small management consultant firm, in conjunction with a larger firm from Washington, D.C., put in a bid on a contract for a personnel development system with the city of Atlanta Board of Education. They, to our consternation—because in personnel services contracts I had not been used to providing bonding, as is done in most construction contracts—demanded 100 percent bonding of a contract that was going to run $100,000–$150,000.

It was just out of the question for us to try to get that done and pay the costs that would have been engendered by it.

Another major problem created by high interest rates is cited by Harry Kaufman, chief economist for the New York-based Saloman

Bros. investment banking firm, as quoted in the Atlanta Constitution on August 11, 1981. Mr. Kaufman stated that inconsistent Federal economic policies and growing competition are a "thundering herd" threatening to sweep local and State governments out of the borrowing market. Cities such as Chicago recently have been forced out of the bond market to wait for a drop in interest rates.

The problems of local governments are further magnified by those facing State governments which must either raise taxes or make drastic cuts in welfare, medicaid, and other social programs in response to heavy Federal cutbacks through block grants. Increased State and local taxes in the form of either sales tax increases or individual and corporate tax increases will hit small business the hardest.

Cuts in funding for SBA-guaranteed and direct loans mean fewer loans are available, ~~and~~ loan rates are so drastically increased as to make them incapable of accomplishing the purposes for which they were intended. Direct loans which were formerly set at 3 percent are now set at the Government's cost of money plus up to 1 percent, for all except handicapped persons. Guaranteed loans are presently set at prime plus 1½ percent. Few small businesses can afford to borrow at this rate.

High interest rates, both for regular bank loans and SBA guaranteed loans, have had little effect on short-term borrowing except for their impact on profits. However, they have had a disastrous effect on long-term borrowing, which is essential to growth, capital investments, updating of plants and equipment, and the formation of new businesses. Large corporations are also affected, but they have access to the bond market and the stock market which small businesses do not have.

The only source for long-term capital for small business during these times of high interest rates has been SBA's guaranteed loan program. Originally such loans were readily available below prime because of the 90-percent loan guarantee. This guarantee has been reduced to 80 percent, and banks are now charging 1½ percent over prime. There should be an upward cap on interest for guaranteed loans. This means the banks or the Government, or both, must underwrite the cost, and we feel it can and should be a shared cost. Bank certification programs should also be expanded and strengthened to cut down on crucial time needed to obtain SBA-guaranteed loans.

While many feel that direct SBA loans should be discontinued, they have been the only source of funds for many new or expanding businesses, especially those owned by minorities or women. This administration has threatened to impound new money appropriated by Congress for direct SBA loans. SBA should work with small business associations, advisory groups, and congressional committees in setting up practical and workable SBA loan programs.

In the area of Government regulations, we realize that some ridiculous rules have been promulgated in the past, but I do not wish to see the wholesale dismantling of regulations whose original purposes are desirable.

We would like to see Government agencies work more closely with businesses and other governments in establishing orderly and reasonable means of achieving these goals.

Three means of Government regulation which have impacted most heavily on business are OSHA, EEOC, and EPA.

OSHA initially failed to set its priorities to accomplish the most important things first. Many of its regulations were costly and onerous and really accomplished little in protecting the health and safety of workers. This is no longer true, however, and regulations substantially affecting the health and safety of workers should be strictly enforced.

EEOC—I do not wish to see us return to the days when companies, large or small, were free to discriminate against applicants or employees on the basis of race, sex, national origin, religion, et cetera. Although small business persons generally support the need for legal aid to assist those who would not otherwise be able to afford legal counsel, we are concerned about the cost to small businesses associated with the filing of EEO and other discrimination cases based on specious charges.

EEOC must remain dedicated to the fulfillment of the purposes of equal opportunity but must make sure that regulations are reasonable and attainable.

I worked for several years on a committee of the National League of Cities studying the proposed guidelines on employee selection, and it will take more of this kind of cooperative effort between government and business to help evolve such guidelines. Changes currently being proposed in the Office of Federal Contract Compliance regulations, that is, no requirement for written affirmative action plans for companies who do not have single contracts involving at least $1,000,000 and 250 employees, may be going too far, however.

EPA—I realize that all EPA laws and guidelines are not equally important. But I am most concerned that we not allow pollution of our water and air so as to create health hazards for ours and future generations, or that we strip our land of its natural resources and beauty so as to deprive future generations of its use and enjoyment.

I was appalled to read in the newspaper recently that a national poll showed businesses most concerned with Federal regulations showed all of them in the area of environmental protection. Many of those concerned the very future of our air, water, and land.

I was, however, relieved to see that the Supreme Court will not allow cost alone to decide which of these regulations protecting our environment are allowed to stand. Again, we must decide what is really important and establish and enforce strong regulations in these areas, while removing those regulations which are not essential to our overall objectives.

Little interest has been shown by the executive branch enforcing the Equal Access to Justice Act, which was passed in 1980. This bill should be conscientiously enforced, and the Congress should extend its coverage to include nonstatutory regulations that are adopted by the executive branch of Government.

Similarly, little has been done to carry out the purpose of the Regulatory Flexibility Act, either in the area of special regulations for small as opposed to large businesses, or in the preparation of economic impact statements prior to the adoption of nonstatutory regulations.

While cost should not be the only guideline in considering such regulations, it certainly should be an important consideration, and provisions should allow businesses to phase in changes and to have flexibility determining which of a number of possible methods should be used to accomplish the purpose of the regulation.

The Federal Government should provide technical assistance and inservice training to small businesses, to help them deal with necessary paperwork and compliance measures required by Federal legislation and administrative regulations.

The Georgia Small Business Council believes that the administration should work with small business associations and congressional committees in evolving programs to aid small business. We are happy to have had this opportunity to express our views to the House Small Business Committee.

We are happy to have the Senate Small Business Committee appoint a National Advisory Board on Small Business, composed of 25 small business owners across the Nation. Two of them are from Georgia, one being Jim Rhoads, now the new president of the Georgia Small Business Council. We also support a strong advocacy program in SBA, such as the original act envisioned and as was so effectively carried out by Milt Stewart. Working together, we can help small business prosper and grow, and we will all be the beneficiaries.

Mr. **Mitchell**. Thank you, Ms. Williams, for very excellent testimony. You covered a lot of ground, and yet it was all very specific. I want to be on record right now, saying I was one of the minority which vehemently opposed these Draconian cuts in the Small Business Administration's programs. It just does not make sense to do it as of this time. However, we were a minority when it came to the vote. We did not prevail in our position. I fear that there will be a similar battle in the second half, a battle to impose even further cuts.

Quite frankly, my position is—as of now at least—that if further huge cuts are imposed on the programs, I would rather see them end. You are whittling them down to where they are meaningless.

I think I might have some bad news for you. Perhaps you have heard that the Federal Reserve has dramatically increased the money supply, dramatically done so. For all of us, that means just one thing: 3 months from now, or 4 months from now, inflation is going to go up again because of the interest rates. No question about it. When you shove out a lot of new money, after a brief timelag, you will see those interest rates go up. That is going to make the condition of small businesses in this country worse, I fear, rather than getting better.

A couple of questions I wanted to ask of you: What, if any, is the relationship between the Georgia Small Business Council and your local SBA State region?

Ms. **Williams**. No direct relationship. They have been most cooperative and helpful with us in getting us started and have attended our meetings and participated in our workshops and seminars. They have been very cooperative.

Mr. **Mitchell.** You pointed out that the $25,000 level is inadequate for used equipment for investment tax credit. What figure would you suggest?

Ms. **Williams.** I don't know that I would be able to give a figure. Perhaps there are others here who have more direct knowledge. My own company is a management-consultant company. I am not myself directly concerned. I am sure there are people on our staff who can give a better figure than that. I will be glad to get their opinion and write it to you.

Mr. **Mitchell.** In your experience, has it been customary to require bonding in consultant contracts?

Ms. **Williams.** No, sir; not in any I have ever done before. This was true in the city of Atlanta Board of Education. It was a personnel service contract. It was to update their personnel system.

Mr. **Mitchell.** I had not heard of bonding being required in that kind of contract. Have you, Major?

Mr. **Clark.** No.

Mr. **Blackistone.** No.

Mr. **Mitchell.** Generally it is limited just to the construction effort.

I like all of your recommendations on pages 3 and 4. They are certainly attractive. I like the idea of exempting from income tax the first $25,000 of profit for a small business which retains the money in the business for capital needs. The problem is, How do we track that? How in the world does any agency of Government say, OK, yes, you can exempt $25,000 as long as you are putting it back in your business. Thirteen million small businesses, 60 million, the idea is attractive, but I don't see how we could work to almost guarantee that there would be no abuse of this. Let's face it: The average businessperson is intelligent and clever.

Ms. **Williams.** If he is going to stay in business very long.

Mr. **Mitchell.** No. 1, I think many such businesspersons would say yes, I am retaining the money in my business, if that is the statement to be made on the IRS form. We just have to take their word. Then if there is some question, I just don't see where the mechanism would come from to really monitor this.

Ms. **Williams.** I think you are right. I think it would be tantamount to exempting the first $25,000, except if they distribute it as profits or anything to investors, that would easily be checked.

Mr. **Mitchell.** There is just one other comment I want to make, then I will see if the staff has questions. You are quite right. It was the House, really, that made the tax bill more attractive for small businesses. There was no real break in the original tax bill that came out of the administration. I do have a concern, and it is a concern that you apparently share. You are pointing out there are certain governmental services that need to be ongoing until we get things straightened out in this country. Yet to the extent and degree that we continue to reduce taxes, that is the same extent and degree to which we jeopardize the ongoing of those services.

Under the present tax bill, when we hit that 3-year-out period, we will lose something like $700 billion in revenues to the Federal Government. I think all of us in this room know what that would mean: further assaults on programs that are necessary just for the survival of people.

How would you personally feel, or has the council taken the position, about the third year of the present tax bill?

Ms. **Williams**. The council has not taken a position. But my personal view is that the third-year tax cut should be canceled.

Mr. **Mitchell**. Thank you

Questions, Steve?

Mr. **Blackistone**. On page 9 of your statement—and I note this statement was prepared in November—you mention the Equal Access to Justice Act and the Regulatory Flexibility Act. You make the comment that little effort has been made to implement both of those pieces of legislation. I am wondering if you have seen any improvement since November in either of those situations?

Ms. **Williams**. I personally have not been made aware of it, if that has happened. As you know, the days before Christmas are not good ones to try to keep up with what is going on anywhere. Also, our more recent snow and ice has kept me from being able to get back and forth to our office to really check on what is going on, so I don't know.

Mr. **Blackistone**. Thank you.

Mr. **Mitchell**. Major?

Mr. **Clark**. Ms. Williams, I have one question.

On page 4 of your recommendations, recommendation No. 3, are you referring to the closed corporation when you state that the number of stockholders allowed in corporations should be increased from 20 to 25?

Ms. **Williams**. Let me defer to Larry Bramblett, from whence this idea came. He knows more about it than I do.

Mr. **Clark**. I can wait until Larry gives his presentation.

Thank you.

Ms. **Williams**. It is those that are not public stock issues.

Mr. **Mitchell**. Thank you very much. It is good to see you again. Thank you for your recommendations. We will look at all of them. I just have the most concern about that No. 4.

Ms. **Williams**. I appreciate, Mr. Chairman, your letting me testify in time to get down and march with the ERA women.

Mr. **Mitchell**. Could you convey a message for me? Right on.

Our next witness is the Honorable Calvin Smyre, Georgia State representative for the 39th District.

TESTIMONY OF HON. CALVIN SMYRE, STATE REPRESENTATIVE, 39TH DISTRICT, STATE OF GEORGIA

Mr. **Smyre**. I have to hurry and testify.

Mr. **Mitchell**. Will there be a vote today on ERA?

Mr. **Smyre**. That will be on Thursday.

Mr. **Mitchell**. We will try to speed up the process. We know where you stand.

Mr. **Smyre**. You are right about that. Right on.

Thank you Congressman Mitchell. It is a pleasure to be here. We thank you for coming to Atlanta to give us an opportunity to express our opinions.

I come to you today as a legislator and also as a banker who is a member of the appropriations committee and also on the Columbus

Chamber of Commerce and who is a partner in Smyre's Supermarket.

The comments I would like to read for the record are on behalf of the legislative black caucus and its 20 representatives and 2 senators. This statement was put together by our staff to show you our plight here in the State of Georgia. We would like this to be part of the record so that for future consideration you all know what our position is in the State of Georgia, and hopefully some relief will be forthcoming.

Mr. MITCHELL. Without objection, your entire statement will be submitted for the record.

Mr. SMYRE. Thank you. It is more than obvious with the growing trend of the State and country that minority businesses will need the continued support and assistance of the Federal Government. In citing you these startling examples, you be the judge, and you be the jury.

In the State of Georgia, the department of administrative services—DOAS—has the entire purchasing authority. While all agencies have been delegated limited procurement authority, DOAS has overall administrative and accounting responsibilities for this function. This authority is granted under chapter 40-19 of the Georgia State law. Under this law over 1,000 State officials have varying powers to purchase during fiscal years 1979 and 1980 over $500 million worth of goods and services.

Georgia State law mandates "that a fair proportion of the total purchases and contracts for property, commodities, and services for the State be placed with small businesses, so long as the commodities and services of small businesses are competitive as to price and quality." But State law has no provision for aiding minority entrepreneurs. Although the vast majority of minority-owned firms are small businesses, most small businesses are not minority-owned firms.

I also would like to add that these 1,000 purchasing agencies have the authority to solicit by telephone nonadvertised bids under $1,000 from firms known to the purchasing officials.

With this bureaucratically controlled process in the Georgia State government, it is who and what you know, rather than free enterprise and competitive market prices.

Mr. MITCHELL. May I interrupt for just 1 minute?

I want to make sure I understand this. As a nonadvertised bid under less than a thousand dollars, a purchasing agent can just get on the phone and say, Jim, you come down and get this one?

Mr. SMYRE. That is correct.

Mr. MITCHELL. Bill, you come get the next one?

Mr. SMYRE. That is correct.

They have never said, "Calvin, come and get it." But that is correct, Congressman. [Laughter.]

Mr. MITCHELL. OK. I will wait. Proceed.

Mr. SMYRE. These two examples show that the DOAS policies and regulations, together with practices of individual State agencies' purchasing officials, tend to exclude minority-owned firms from doing business with the State of Georgia. As of this date, minority businesses this fiscal year will receive less than 1 percent of all goods and services purchased by the State through DOAS.

The total dollar value of State contracts for fiscal year ending June 1981 was $257 million, with minority businesses receiving $2.4 million, which is 94 percent of 1 percent. You be the judge, and you be the jury.

In the State department of transportation, DOT, their procurement contracts from minorities have increased, but it is still a dismal sight. The total contracts for DOT are over $300 million for fiscal year 1981, of which approximately $12 million went to minority contractors. The largest of that went to subcontractors and is attributable to the Federal Government having a minimum of 2 percent on all federally aided contracts. It is obvious, with the results as I have stated, that minority businesses will need the continued support and assistance of the Federal Government.

With the support and assistance of the Federal Government, minorities have been able in the last decade to get their foot in the door. The support has come from endorsing legislation for set-aside programs for minorities and helping to enforce the suggested changes after their acceptance, as a direct result of a set-aside program. Emphasis also should be given for the continued support on the Federal level to the Small Business Administration. Example: SBA loans, 8(a) contracts, and bonding.

In the year ending September 1981, SBA figures showed 3,687 loans totaling $143 million made to minority businesses, which represented 6.29 percent of all loans made in the United States. In the State of Georgia, my concern is that the State received $1.1 billion in Federal contracts for fiscal year 1980, according to the Department of Commerce's Journal of Minority Business. Of that $1.1 billion, minority businesses received $38 million, or 3.3 percent.

Georgia ranked No. 13, percentagewise, of all States reported. The State, however, was ranked eighth in the number of minority businesses. With 12 military installations and 9,728 minority businesses, it appears that the State should rank higher than 13th in the number of contracts awarded. More emphasis should be placed on support for the number of minority businesses in the State as well as the number of contracts received in fiscal year 1980.

Finally, we need more assistance from the Federal Government in bonding. Bonding guarantees are nonapplicable through SBA. The SBA has helped minority contractors with their bonding assistance. As a result, more minorities have gotten more jobs. There are a lot of complications, as you know, involved in obtaining bonding, and historically minorities have had more problems than others. With the continued support from the SBA for their bonding program, more minorities will secure contracts in the future.

In reality, and being realistic, our present condition is defined as the calm before the storm. Except for Public Law 95-507, the set-aside program and the SBA 8(a) program. We are at a disadvantage, and it seems as though history may repeat itself. There is a hostile threat in this country to our minority economic development interests.

When minority business enterprise performance is compared to the mainstream business community, the figures, as you know, are shockingly deficient. While minorities represent 1 out of every 6 Americans, we participate in only 1 in every 152 business enterprise dollars received in this Nation. Minority business receipts from the 8(a) program represent a meager $1 for each $1,667 of the total national business receipts. What these figures really say is that under present conditions we do not have the capacity to make the free enterprise system work within the minority community. I am suggesting that the SBA 8(a) program be enhanced because there is a need for a vehicle for continued negotiated procurements in the future.

It also appears that the application of small business set-aside procedures to the special needs of the minority business community will greatly enhance and expedite minority business development as a meaningful economic force within the minority community.

This is the conclusion of the statement, Mr. Chairman.

Mr. Chairman, those of us here feel that the State of Georgia is in a dismal state at this point in time. Those of us in the legislature who are on the appropriations committee and the ways and means committee and the DOAS Subcommittee of Continuation and Out-Budget Procedure, feel it is unfair as it is now processed in the State of Georgia.

We have tried in the past with legislation. We have adopted the State law of Maryland and Florida and the State of Ohio and sort of have incorporated the changes and the procedures that you all adopted in those various legislatures and tried to come up with a comprehensive vehicle that would be adaptable to the State of Georgia as far as public policies and rules and regulations are concerned.

At this time, the legislation is still in committee. We have two pieces of legislation: One dealing with regular government and one dealing with the DOAS, which is our purchasing agency. To this date, we have not been able to get the bills past the house. We got a vote on the floor of the house. It was sent back to committee with no recommendation. Our efforts again will be trying to come up with a program that we think is fair and can be compatible to all and could enhance our position here in the State of Georgia.

Whatever assistance that you all could provide to us through SBA and through other Federal procurement programs would certainly be of help to us. We congratulate you on the work that you have done in the past, and we look forward to being in a partnership with you in the House and the Federal Government in the future.

Mr. MITCHELL. Thank you very much. You don't meddle in the internal affairs of a political subdivision. I am curious, does your legislation, which will apply to DOAS, address this situation on page 1? This under $1,000 telephone bid contract?

Mr. SMYRE. It will increase it. Because of the nature of the legislature and the difficulty they are in, you know the different political philosophies. That part of it was one of the mainstays of the legislation, but we have agreed and did pick up votes that if we would increase it, we would not increase it more than $5,000. As you know, there are over 1,000 purchasing agency officials. You are dealing with those agencies that have friends in the legislature. It makes it very difficult to fight them, so to speak. We have come up with a compromise.

Mr. MITCHELL. You see, my problem is that those are the exact kinds of contracts that the little guys would want to go for, $1,000 and below, $5,000 and below. If they are frozen out of the system, there is no way in the world—I am not saying it is—this is one of the institutionalized practices that I think does not inure to the benefit of minority businesses and small businesses, the same kind of institutional practice that exists in the private sector where we have subcontracted with this guy for 15 years and therefore we will continue to subcontract with him even though we have a greater volume of business to subcontract.

Good luck with that one.

Mr. **Smyre**. Thank you very much.

Mr. **Mitchell**. I don't have any questions. There was one other comment I wanted to make. Let me find out where it was. I just wanted to comment with reference to the continuation of programs which are now in place. I pledge to you, as chairman of this committee, we will continue to work to keep those programs in place, and hopefully to begin to fund them again at an adequate level. The answer to me, in terms of the 8(a) program and forced graduation is not to be found in the present practice. You do it at the other end.

Congressman Gingrich said you want more firms to participate; and someone else alluded to that, too. I think you did. The way you do that is to broaden the number of opportunities at the Federal level rather than squeeze people out. Sure it is true that only 2,000 firms are presently in the 8(a) program. I think it is about 2,000. If we would make these agencies open up more contracts, or if we would merely implement Public Law 95-507, there is an enormous opportunity to double the number of 8(a) firms, provided of course SBA got the personnel that it needed to do that. I think it is the wrong way to do it by forcing firms out into what is guaranteed failure as opposed to enhancing the opportunities by letting more contracts be made available to 8(a) firms.

Thank you very much for your testimony.

Mr. **Smyre**. One of the problems I mentioned, alluded to, was the bonding. I heard the gentleman earlier allude to the fact money had given out earlier. He knew of an example. I know a couple of times that persons were at the point of contractual agreement. The bonding capabilities were not there. SBA could not give that relief. Those are the types of things.

Mr. **Mitchell**. You trigger me to make one more comment which I didn't want to do. I have found that these new policy changes initiated in Washington are done almost without any consultation to a regional office or field office, and, therefore, many of them have no idea what the impact of that policy would be.

I think the bonding thing is a clear illustration of it, the fact there was a moratorium imposed almost arbitrarily, somewhat capriciously, maybe not in Georgia, but in another region. There was a guy all set; he got locked in with a private firm finally. It was OK. The firm put it in writing: "OK, just as soon as you get your 8(a) certification, we are in business." Then a moratorium arbitrarily and capriciously was imposed.

I don't know how we will tackle this problem. I am frank in saying this: I have been in Washington 11 years. This has not been the kind of problem that has occurred under the last four Presidents. Under President Nixon there was at least consultation with the regional and local people to see what this policy would mean before it was put into effect. Now I find that many of the agencies of Government in Washington, and SBA in particular, have gone ahead and simply implemented policies without attempting to assess the impact of those policies at a local level, and people have been hurt.

Counsel?

Mr. BLACKISTONE. Thank you, Mr. Chairman.

Is there legislation pending now in the Georgia Legislature to embody the Reagan administration concept of urban enterprise zones?

Mr. SMYRE. If you speak of legislation, there is not legislation per se. The concept is being studied and looked at. I was scheduled to testify and did make some comments over the telephone to the Associated Press on urban enterprise zones in reference to the hearings Senator Mattingly held at the Federal building a week ago. We were in session, and I could not make it, but there is a concept there that some of us who would like to take a strong look at enterprise zones are looking at it, but we have not come up per se with legislation that would pertain to the State as yet.

Mr. BLACKISTONE. Could you, on the basis of your initial exploratory investigation, make any suggestions on how they ought to be formed? What kinds of incentives ought to be used; how best to manipulate the tax and regulatory schemes to make it something that is truly effective?

Mr. SMYRE. Not being knowledgeable of it in its entirety, I will make this comment, though. Based on what I have heard and from the urban officials I have talked with, and the people that handle our tax programs within the house on our ways and means committee, the tax incentives would, at this point in time, be a disadvantage to the State per se rather than a value that it may bring.

I have talked with a couple of mayors that would like to see enterprise zones, but they don't know whether or not we could take the load by providing the tax incentives or not. We have gotten some feedback.

If you remember Freeport, when Freeport came about, take the tax loads off of inventory goods in terms of inventory that was placed in warehouses at year's end. We found out basically the big businesses were inventorying it at the last part of the year to get the front end off. The next thing you know, the tax base had been cut for a particular municipality because of a company getting a large-scale inventory for yearend for the next fiscal year. Those are the types of things you have to look at in terms of your tax base. When you do that, you put a larger role on the regular property tax. That is when you have your political problems.

Mr. BLACKISTONE. Thank you.

Mr. MITCHELL. Major?

Mr. CLARK. No questions.

Mr. SMYRE. Tell Clarence I said hello. We were happy to have you in Baltimore with us.

Mr. MITCHELL. Have your next convention there again.

Thanks. Good success to you in the future.

I would like to call Larry Bramblett as our next witness.

I want to embarrass him as he is coming forward. I was at the University of Georgia at a conference Mr. Bramblett and others put on. I think the best testimony of a person's commitment comes from those who sought service and assistance. There was enormously high praise for you by the business people at that conference. They said you were one of the sincere ones. I think that ought to be on the record.

TESTIMONY OF LARRY R. BRAMBLETT, DIRECTOR, SMALL BUSINESS DEVELOPMENT CENTER, UNIVERSITY OF GEORGIA

Mr. **Bramblett**. Thank you, Mr. Chairman. I appreciate that.

We prepared a formal statement for the earlier hearing. Due to the weather or some other factors, it appears that the U.S. Postal Service did not get the statement to your staff here in Atlanta. What I am prepared to do this morning is make some summary statements. We have just completed under the auspices of the State Senate Small Business Study Committee, soliciting the views and recommendations and opinions of approximately 1,400 to 1,500 small businesspersons in the State of Georgia; so I am going to talk about some of those findings.

However, as you are aware, I first must talk about the small business development center program. I would like to essentially address that from the national level and then digress to our State situation.

As you are aware, Public Law 96-302 was finally passed in Congress after great debate and Presidential veto in 1980. Within Public Law 96-302 is the Small Business Development Center Act, which calls for local institutions, be they public, private, State, or whatever, to provide counseling services, continuing education services, information transfer services, and advocacy-type services, to the small and minority business sectors of our Nation.

Obviously July 1980 has not been that long passed. However, there was an administrative-type program begun in 1977. In the State of Georgia, our general assembly passed, prior to the initiation of a national program, enabling legislation which allowed us to begin in April 1977.

Our program, Georgia SBDC operations and those nationally focus essentially on providing managerial assistance in the areas that I previously mentioned. From the national perspective, the Federal Government is spending approximately $8.5 million on this program. It is now situated in 19 States and the District of Columbia. As was reported by the Regional Administrator of the SBA, during the preceding testimony a congressional sunset analysis or audit of the program will be conducted by January of next year. However, I think it would be appropriate to reflect on some of the accomplishments of the program to date at this time. In the area of counseling, the Small Business Development Center network nationally has, in the last 12 months, provided counseling services for 18,787 firms; the total direct counseling hours equaled 229,000-plus hours.

In the area of information transfer, the Small Business Development Center network will touch over 100,000 small firms annually. By information transfer, I am referring to data that we in public institutions and large corporate bureaucracies have readily available to them—decisionmaking-type information that is transferred via the SBDC to small business. In the continuing education area, the Small Business Development Center program reached this year roughly 100,000 persons. In the area of advocacy, which is a role that has not been one that universities have traditionally worked in—universities have traditionally maintained a platform for debate—the universities are moving out in the small business areas as advocates for small business because it is in the national interests economically for them to do so.

One excellent example of what can be done in this area, and what is being done could be taken from our State. Our office of minority business development has been very instrumental in forming a Georgia Association of Minority Enterprise Organizations, which, in fact, will hopefully become the political voice of the minority business community of this State to the State legislature and to our Congressmen and Senators from Georgia and to the executive branch of the National Government.

In addition to that, the Small Business Development Center, through the office of minority business development, has been very instrumental addressing the very issues that Representative Smyre mentioned just a few minutes ago with State purchasing. We think we are going to have some influence on the level of contracting between State government and minority businesses.

Fifth, Small Business Development Centers are beginning to engage in entrepreneurial education not only at the postsecondary level, but also at the high school and elementary level in public schools. Roughly 65 percent of the population of high school graduates in the United States, those high school graduates that graduate during the current decade, will have to find employment in, own, or manage a small firm if the unemployment rate stays below 10 percent in this Nation.

At the same time that this situation appears eminent, public education at the elementary and secondary level, by the way, at the vocational level, and in many cases at the postsecondary level, no training whatsoever in the small business or management area is offered. SBDC's are working and beginning to broaden work in this area with public school teachers and the like to prepare our youth, for what will be their occupational career choice.

In terms of the economic contribution of the SBDC program, numbers and philosophies and concepts do not mean very much unless they can be implemented. Perhaps we can extrapolate the Georgia experience for this status report on the SBDC program; $8.5 million is being invested nationally in the small business development program. In Georgia alone, domestic sales have increased $200 million annually among clients served. In terms of export business sales, roughly $20 million is being created annually by the Georgia program. In terms of jobs created in the Nation, we believe that approximately 12,000 are being created annually. Georgia contributes about 10 percent of that amount.

In terms of jobs saved by SBDC's, we are looking at approximately 17,000 of Georgia's SBDC saved, again, roughly 10 percent of the private sector jobs. In terms of business profits—and this gets down to the bottom line and to the tax line—approximately $180 million in net profit before taxes are generated nationally through the national network.

I would be remiss not to take this opportunity to make some suggestions. I would like to make one recommendation for consideration to the committee and to you, Mr. Chairman, with regard to this, the SBDC program nationally. Then I need to talk a couple of seconds about some of the recommendations that have come out of the Senate's Small Business Study Committee here in Georgia.

Public Law 96-302, the Small Business Development Center Act, was greatly debated, studied, and analyzed by the 94th, 95th, and 96th Congresses. That law is a very effective law, and I would ask you, the committee, to attempt to insure that the administration and the agencies there implement that law as it appears on the books. With respect to that matter, the law calls for a national director of the program. Obviously appointment has not been a very high priority of the agency. Therefore, we have no national director after over 1½ years in operation.

Second, it calls for a national small business advisory board to sit over, and make recommendations to, the SBDCs and to the Federal Government on the directions the program should take. This advisory board to date has not been formed.

Third—and I think this would need looking at very closely—there is a funding formula imposed in Public Law 96-302. This funding formula is not being adhered to nationally. I recommend that the funding provisions of the law be enforced by the Congress.

Mr. MITCHELL. Could you give me a little more detail on the formula?

Mr. BRAMBLETT. The population formula, sir, requires a 50 percent State or local match as a minimum. The formula derived by dividing the national population into a State or local entity population and may be described as a regional entitlement. The entitlement and the funding divisions among programs are not being adhered to across the country. They are in some cases understated and in some cases overstated with respect to the actual budgets, the actual grants that are distributed.

Mr. MITCHELL. In the State of Georgia you have a matching formula. Right?

Mr. BRAMBLETT. That is correct.

Mr. MITCHELL. Fifty-fifty?

Mr. BRAMBLETT. That is correct.

Mr. MITCHELL. The State comes up with its 50 percent?

Mr. BRAMBLETT. That is correct.

Mr. MITCHELL. Are you telling me that the Federal Government then is now giving not its full 50 percent, but 30 percent of the 50 percent it might give?

Mr. BRAMBLETT. Roughly 29 percent for this State. We have a population approaching 6 million, right at 6 million people. If you take that nationally, we are supposedly entitled in the national budget to roughly 1.75 percent of the national budget at the full funding level, which was estimated to be $50 million by the Congress in 1979-80.

Mr. MITCHELL. Has that been ongoing since the beginning of this program?

Mr. **Bramblett**. That is correct. There is a need to review that funding situation.

Mr. **Mitchell**. All right.

Mr. **Bramblett**. On other matters other than Small Business Development Center Business, Ms. Williams, with the Small Business Council, made recommendations in several related areas. Congressman Gingrich discussed some of these areas. Reflecting from a national perspective what our State study of approximately 1,500 small firms have said that needs to be done nationally and at the State level, needs to be presented.

Number one, as everyone has pointed out, we need to encourage equity financing of small business through tax-exempt investment programs. We need to change some of the prohibitions of the SEC regulations. We need to expand similar programs to that of the SBICs.

In terms of the comment that was made, the question you asked of Ms. Williams, she was referring to the 15 limit that is currently imposed by the SEC on public corporations in the state exemption. It would be more effective in many cases of small business firms, much more equity capital could be found if the number of investors were permitted to increase without forcing a small firm to go public. We understated significantly the cost. The cost is well in excess of $100,000 now. Well, in excess of that.

In relation to the other comments that the Georgia small business community made in regard to these hearings, Congress is certainly going to enforce the Regulatory Reform Act, which comments have already been made about. Yet I hasten to report to you that the State of Georgia's regulations and redtape now far surpasses the Federal Government's. So these small firms are speaking out in terms of an overall picture, not necessarily a picture coming directly from Washington. When you hear about redtape find out what redtape from whom.

They certainly encourage through special grant programs entrepreneurial education from the national level to prospective owners and managers of small business through the public education system. Again, small businesses in Georgia have suggested that a tax-exempt status for small businesses that have an annual net income of under $25,000 be given a tax-free status. Now, I don't know whether $25,000 is the figure or not, but that is the figure that is being kicked around here.

Fifth, they have suggested that at the State and the Federal level that a 2-year income tax moratorium be put on new small businesses, the baby ventures.

I would say that suggestion has fairly significant pitfalls and carefully prepared statutes would have to be written, because you would have new businesses going and coming everyday to qualify under this proposed exemption. But that potential problem could be handled effectively.

There is a significant need to maintain equity capital in a firm that is 1, 2, 3, 4, and 5 years old. I don't know where the cutoff year should be. The first 3 years are very, very critical. We are finding in the Small Business Development Center, if they get past the 3d year, generally speaking the survival rate increases geometrically. It is those first 3 years that are quite critical.

The small business community of Georgia urges that you allow small firms to expense assets up to $50,000 per year.

These business persons also point out that we need a very strong exporting program. That is where the paybacks really are. The domestic, as great and large as it is, does not offer as great a potential as resides in the market place of developing nations of the world for perhaps a great percentage of small and medium-sized firms in the United States, the greatest market potential is in exporting. Finally the small business community of Georgia recommends the expansion of the Small Business Development Center program. They recommend to you, too, that you, the Congress, would pass some sort of legislation that would require that the President report to you the amount of business that small and minority businesses do with the Federal Government annually.

With respect to Mr. Smyre's remarks about State procurement in Georgia, I think there is probably great potential—maybe not in this session, but in the next session, I think there is great potential in this State for enabling procurement legislation being acted upon, that will require the chief executive officer to report the exact volume of business that was done and that some goal, some executive goal, be set on that annually, similar to the role, or the approach President Carter used in his years as head of the national Government.

[Mr. Bramblett's prepared statement follows:]

PREPARED STATEMENT OF LARRY R. BRAMBLETT, DIRECTOR, SMALL BUSINESS DEVELOPMENT CENTER, UNIVERSITY OF GEORGIA

SOME REFLECTIONS ON SMALL BUSINESS AND THE SMALL BUSINESS DEVELOPMENT CENTER PROGRAM OF GEORGIA

Introduction

The purpose of this work is to share with the United States House of Representatives Small Business Committee some of the more pertinent information regarding the small business community and the Small Business Development Center program. This work is not intended to be comprehensive. It does however, address matters that expand over a four year period.

The contents of this presentation are given in outline form and are divided into the following categories:

A. Economic profile of small business in Georgia.

B. Biographical, psychographical and behavioral information on small business in Georgia.

C. The Small Business Development Center program—what has been learned, what has been proven.

Economic Profile of Small Business

Small business in Georgia provides employment, economic freedom and life-improving innovations to the extent that the welfare of every citizen of the state is affected. In short, "so goes small business, so goes Georgia." The latest statistics reveal that 64.73 percent of the total private sector payroll is drawn from firms with fewer than two hundred fifty employees. Note, this percentage does not take into consideration the thousands of self-employed professionals, farmers and small business persons. Thus, it is conservatively estimated that over 75 percent of the households in Georgia draw some or all of the family income from a small for-profit enterprise. The majority of families not employed by government draw the bulk of the family income from small businesses or from self-employment.

In terms of bodies, the total private sector labor force consist of approximately 1,707,447 individuals. Small business employs 1,190,166 persons.

This represents 70 percent of the total private sector labor force. Another eight percent of Georgia's labor force is self-employed. Thus, big business provides approximately 22 percent of the private sector jobs. In terms of number of establishments (excluding self-employed) the government employs 14.5 percent of the labor force. For statistical purposes, a small business is defined as an organization with less than 250 employees. Self-employed persons are not included. Roughly 98 percent of all businesses in Georgia are small. Even more interesting, is the fact that the annual payroll for firms with 90 or fewer employees is almost identical to firms with more than 500 employees. Further, businesses with less than 100 employees met sixty percent of the annual payroll in Georgia. Finally, it is revealing to note that only 97 businesses in Georgia employ over 1,000 persons.

A comparative rating can be made among the major industry sectors using both employment and payroll information. This is given as follows:

Figure I

Industry Category	Percent of Total Employment	Industry Category	Percent of Total Payroll
Manufacturing	31.433	Manufacturing	33.898
Finance, Insurance & Real Estate	19.998	Wholesale Trade	15.201
Wholesale Trade	18.385	Finance, Insurance & Real Estate	13.259
Retail Trade	8.509	Transportation & Other Public Utilities	11.113
Transportation & Other Public Utilities	7.392	Retail Trade	11.157
Services	6.571	Services	7.382
Contract Construction	6.237	Contract Construction	6.418
Mining	0.429	Mining	.055
Agricultural Services, Forestry, Fisheries	0.372	Agricultural Services, Forestry, Fisheries	.029

Source: Georgia Econometric Forecasting Project and County Business Patterns

Exhibit A, found at the conclusion of this section, gives in more detail statistical information on each major industry sector in Georgia. In terms of employment growth covering the five year period of 1975 through 1979, industry descriptives are given as follows:

1. Agricultural employment grew by 45.80%.
2. Wholesale employment grew by 34.09%.
3. Transportation grew by 26.20%.
4. Finance, insurance and real estate grew by 25.97%.
5. Manufacturing grew by 25.17%.
6. Retail trade grew by 23.46%.
7. Services grew by 22.74%
8. Contract construction grew by 20.82%.
9. Mining grew by 5.25%.

Overall, employment in Georgia grew at the rate of 5.23% per year, while the private sector payroll increased annually at 12.976%. Thus, below average employment growth was recorded for the industries of manufacturing, retail trade, service, contract construction, mining and finance and insurance and real estate.

What do all of these figures tell us? Well, statistics generally tell one what one wants them too. The only growth factor that is worth noting is in the agricultural services, forestry and fisheries industry and in real employment, that growth rate was nominal.

With reference to small and large businesses, employment in organizations with 500 or more employees grew over the five year period by 21.27 percent while firms with 19 or fewer employees had an employment growth of 18.46 percent.

Firms with 20 to 99 employees experienced a 32.29 percent increase in the number of employees.

Minorities make up almost 17 percent of our population, however, minority-owned enterprises account for only 5.7 percent of the total number of sole proprietorship partnerships and small (sub-chapter S) corporations, and for only 3 percent of total gross business receipts.

New Job Generation

The small business sector employs more than half of all working Americans and these firms are providing most of the new jobs in our economy. According to David Birch of the Massachusetts Institute of Technology, firms with fewer than 20 employees create most of the new jobs generated. Birch's data is summarized as follows:

Firm Size	Percentage of New Jobs Created
0 - 20 employees	66.0
21 - 50 employees	11.2
51 - 100 employees	4.3
100 - 500 employees	5.2
Above 500 employees	13.3

With reference to Georgia, these national statistics may have several implications. First, it has been observed that firms in the state with 500 or more employees are expanding employment at a rate of better than 4 percent per annum. With respect to the national situation, the question must be raised as to whether these are new jobs or jobs acquired from big businesses transferring to the South. If the latter happens to be the case, then it would appear that upward adjustments in the cost of doing business in Georgia will occur. This factor, coupled with more aggressive competition from other states around the nation, may eventually erase the edge off of the present competitive advantage that is now enjoyed.

Innovation/Competition

Small businesses, like other sectors of the economy, operate in a highly competitive environment in close proximity to customer needs. However, there does exist a difference in the environment of small organizations and larger ones. Smaller firms, due largely to the lack of bureaucracy, respond more rapidly to market needs. Small businesses, on a dollar-for-dollar basis, produce 24 times more innovations than do larger organizations. Furthermore, approximately half of the U. S. technological advances in this century have originated from individual inventors of small companies. The Xerox copier, the Polaroid camera and the 6502 Micro Processor are three examples. The latter may have as much influence on our lives as any innovation in the last half of the twentieth century.

Biographical, Psychographical and Behavioral Information

Biographical Information

This section of this presentation presents, in summary form, a biographical profile of small business in Georgia.

1. There are slightly over 110,000 small business establishments and self-employed persons in the state.
2. The growth rate in the number of firms increments at approximately one new business with the addition of 25 persons to the population base.
3. In any eighteen month period roughly 20 percent of existing small businesses are no longer in existence. In the same time period, there will be slightly over 20 percent new ventures started. Collectively, this represents a forty percent change in the names, places and faces of small businesses.
4. The total number of women going into business equals roughly one-third the total population of new ventures.
5. The failure rate of minority firms is higher than the failure rate of non-minorities.

6. There is no significant difference between the failure rate of female owned firms and male owned firms.

7. The growth peak for female owned firms is less than that of male owned firms.

8. Approximately seven percent of the firms in Georgia are minority owned.

9. Small and minority businesses cease to borrow long term capital to enhance business growth at an interest rate near or below 15 percent annually.

10. Small businesses curtail short term deficit financing near the 15 percent interest rate.

11. Generally, small and minority businesses have no formal managerial training.

12. Entrepreneurial type small business persons possess and demonstrate the following traits:

    a. single mindedness.

    b. work diligently and sacrifice greatly for goals.

    c. great amount of self-confidence.

    d. take a good idea, service or product and do something about it.

    e. great amounts of energy.

    f. accept financial risks and personal humiliation.

13. Small business persons are not walking encyclopedias of business knowledge and information. Yet, they are asked to be to survive.

14. Small business persons are not widely traveled.

15. Small business persons are good citizens of the community, the state and the nation.

16. Small business persons pay most of America's bills.

The Small Business Person's Environment

The world of a small business person is not neatly organized and specialized. Diversity and change dominate the clock. Time and knowledge are the two most precious resources of the business owner.

The success of a small business is greatly dependent on big business as either vendors or customers. Also, the small business is heavily dependent on the banking community. Further, small business is badgered by the state and federal government with regulations and taxes.

Through years of apathy, abuse and overload, alienation is accruing. Also, the mass of artificial disincentives that have been created discourage development and growth of new and existing small business.

The Small Business Development Center Program—Observations Thereof and Contributions Thereof

Observations

1. Regulations at the state level are more burdensome on small business than federal regulations.
2. Taxes at the state and national level are biased in favor of big business and big government.
3. The federal government and the state government conduct only a nominal amount of business with small firms.
4. Small business persons are pooly trained and possess too little information to make prudent business decisions.
5. The public education system of the United States is aimed at meeting the needs of big government and big business.
6. Given adequate training, counseling and information, the small business survival rate can be enhanced significantly.
7. There exist a dearth of equity capital for small business.
8. Financial institutions are not totallv effective in providing for the capital needs of black owned businesses and female owned firms.

9. Only limited efforts are being made by both the public and private sector to enhance small business growth.

10. The SBA operated loan program is heavily biased toward land, equipment and building. The program does serve a useful purpose, providing long term capital.

11. States and communities are willing to share in the costs of providing counseling information and training services to small businesses.

12. Small businesses are not reluctant to request these services from universities.

13. Due to the existence of a vast pool of business resources and the position of the university in the community and state, higher education is capable of delivering high quality services to small businesses more economically than other known delivery systems.

14. Like any good bureaucracy, the SBA, nationally, has worked diligently to foster the bureaucracy's growth and to protect the turf thereof, at the expense of the small business community and the American taxpayer.

15. In addition, the SBA has strived diligently to make the SBDC merely an extension of the same organization.

16. The SBA is a numbers agency (quantity oriented) and this is reflected in the MA and SCORE programs. Quality and impact appear to be dimensions that are frequently overlooked as given by the Rockville Report.

17. In general, the SCORE program is poorly coordinated and managed.

18. The many shortcomings of the Agency appear to relate to the depth of organizational focus and to an abundance of personnel who are under-motivated and undertrained. Simply stated, the organization appears to attempt to do too little for too many with under qualified personnel.

SBDC Contributions Federal Fiscal
Year Ending September 30, 1981

The Small Business Development Center of Georgia was established in April 1977.

Any public or private supported organization should be judged based on the ability of the unit to contribute to society. The standard dimension of measurements should be costs, quantity, quality and impact (CQQI). The costs associated with the services offered by an organization should represent the most efficient way of delivering said services. The quantity of services delivered by a particular organization should be easily acceptable and available to all who have needs. Concurrently, the quality of the services provided should offer satisfaction. Also, these services should provide results.

The Georgia Small Business Development Center case for the previous federal fiscal year is present as follows:

Counseling and Information Transfer

Three thousand five hundred (3,500) business clients received assistance of a management or technical nature through the Business Information Services Program of the SBDC during 1980-81. Thirteen hundred forty-nine of these clients received an average of 15 hours each of free professional counseling services. Approximately twenty percent of these clients were minorities. Thirty percent were women.

Lifelong Learning

Another major thrust of the SBDC is to provide lifelong learning opportunities for Georgia's thousands of existing and potential small business owners and managers. During 1980-81, the SBDC cosponsored two hundred ninety-four (294) courses, seminars and workshops in thirty-six (36) locations throughout the state of Georgia. These programs were attended by nine thousand eight hundred fifty-seven (9,857) participants.

Two hundred twenty-eight (228) of the above courses were offered in the Small Business Development Series. This collective offering included sixty-eight (68) different subject areas. These programs were attended by six thousand four hundred twenty-one (6,421) participants.

Expanding the Knowledge Base Surrounding Small Business

SBDC faculty and staff continued research efforts in the area of small business. More than two dozen projects were undertaken during 1981. Under the direction of Wray Buchanan, a comprehensive organization and education needs-analysis-study for the real estate industry of Georgia is being conducted. Hopefully, this work will assist in guiding several thousand firms through what appears to be a very uncertain transition period.

Advocacy

During 1981 the SBDC engaged in a number of advocacy-related activities. Two of the more formidable efforts resulted in the establishment of two Georgia-based small business associations.

The Georgia Association of Minority Entrepreneurs (G.A.M.E.) was formed in January 1981 as a result of efforts of the Minority Development Office of the SBDC. This advocacy organization represents approximately eight to ten thousand minority businesses in the state of Georgia.

The Georgia Small Business Council was established. This advocacy organization has the potential of uniting all of small business in Georgia for the purpose of influencing government at the local, state, national and federal levels.

Small Business Cooperative Education

The business student Cooperative Education program which was initiated in 1978-79, continued to show remarkable growth. Ninety-five undergraduate students were placed in businesses during 1980-81. Many of the problems associated with small business would be alleviated if well trained young adults were to filter into the rank and file of small firms in Georgia. Of all the students graduating from a public secndary institution in this decade, 70 percent will either work for a small business or own a small business during their careers. Yet, few of these youth will receive any formal business education.

Table I
Return on Investment for Taxpayers of SBDC Programs in FY '81

Economic Category	Direct Contribution of the Center
Domestic Business Sales	In excess of $150,000,000
Export Business Sales	In excess of $20,000,000
Jobs Created in Private Sector	In excess of 1,200
Jobs Saved in Private Sector	In excess of 1,700
Business Profits Before Taxes	In excess of $18,000,000

From the information provided in Table I, an estimate can be made to determine tax receipts generated by the SBDC program. During FY 1981, the Center created in excess of $30 million for the public's treasury chests. This represents more than a 14-to-1 investment return ratio. Simply stated, for each dollar of public funds invested in the SBDC in FY '81, more than $14.00 was returned to the public before twelve months had lapsed. It is worth noting that the multiplier effect was not used in calculating these estimates.

Recommendations to the Federal Government

1. Encourage equity financing of small business through tax exempt investment programs, changes in prohibitive SEC regulations and expansion of programs similar to the SBIC's.
2. Enforce the Regulatory Reform Act and the equal access to justice statutes recently passed by the Congress.
3. Encourage the development of entrepreneurial and small business education programs for the nation's youth through grant programs to the states.

4. Establish a tax exempt status for small businesses that have an annual net income of under $25,000.
5. Establish a two year income tax moratorium on pure new corporate ventures.
6. Allow small businesses to expense assets up to $50,000 per year on new asset purchases.
7. Encourage small business exporting through programs of in-depth counseling and information transfer in the export area.
8. Encourage minority small business development through programs of in-depth counseling and information transfer.
9. Expand the Small Business Development Center program to all fifty states.
10. Require of the President of the United States an annual report to the Congress on the amount of business the federal government conducts with small and minority businesses.

Mr. **Mitchell**. Thank you, sir.

Again, your No. 6 recommendation, how do we monitor this? If we start to move it up to $50,000 a year for each new asset purchase, most people are honest, but when you get into the problem of tax law and making changes in it, you almost have to try to assume there is going to be 100 percent real compliance. How would you monitor this? Would you spotcheck every 20th firm, or something like that?

Mr. **Bramblett**. Mr. Chairman, that, I think, would be the only way it could be handled. I think you would certainly not want to create a bureaucracy or additional paperwork that perhaps would cost more than the benefits to be derived from the program.

Yes, sir, that is what I would recommend that you do.

Mr. **Mitchell**. Who might do that? IRS, I guess.

Mr. **Bramblett**. IRS is set up to do that, sir.

Mr. **Mitchell**. Fine. Let me just indicate to you that on your recommendation about expanding the Small Business Centers to all 50 States, I think that might be a good idea. So far in this administration, I have not seen much evidence of a kind of vocal support for the Small Business Development Centers. I think the funding is OK for the next fiscal year for those centers, but I have not heard nor seen any evidence from the administration that it is supportive of the whole concept of the Small Business Development Center.

I think the funds were actually gotten there by the Congress. I am reasonably certain there was an effort made by Mr. Stockman to, if not eliminate them, decrease the funding significantly. What I am saying is, I don't think it is reasonable to assume an expansion right now. I think it is reasonable to try to hold onto what we have got.

Mr. **Bramblett**. Mr. Chairman, you raised the question about meeting with OMB. There is a philosophical question; maybe it is not philosophical; maybe it is an economic type question. I am not convinced that the supplysiders, if you will, totally understand that small business in the free enterprise system, given all the artificial barriers we have created over the years, can, in fact, carry the burden in the purest sense. Obviously we all agree that the Government should not do it for us, but there has to be an environment conducive to a transition period to the supply side.

I am not sure from my conversations with Reagan officials that this factor is totally understood. A program like the Small Business Development Center is not a handout. It is actually returning to the Federal Government's treasury chest far more dollars each year than it is taking out.

Beyond that, and this relates to the 8(a) program, to bonding, a number of other things—if, in fact, inflation and high unemployment is of national concern, then this program should be maintained. If we do not have—regardless of the funding, regardless of how free everyone is to go seek and do what they want to do—if they don't have the skills to do it in a competitive environment, competitive compared to the Government or competitive compared to the large corporations, then it is not going to work. I would encourage the even further managerial type assistance to be attached to the 8(a) type programs we have.

Mr. **Mitchell**. I am sorry; I did not hear that.

Mr. **Bramblett**. I would encourage extended managerial assistance be associated with the 8(a) program. In terms of a cutoff on that, you have asked that question. I don't know if there is a definitive answer. Graduation, certainly you agree with that principle that there should ultimately be a graduation, but there is a problem. The problem is there should be an effective beginning and an effective ending of the beginning. Who knows how long it will take to get this question appropriately answered? There have been no experiences, no cases.

If you go to the insurance agencies, you can check the bonding records, and you find right now that a firm that is being bonded the first 3 to 4 years, their record there is such that the insurance companies claim that they are not making any money at all in that bonding market. So that would lead you to believe that, if you turn that program loose in the earlier years, that there would be no chance for survival.

Mr. **Mitchell**. Thank you very much.

Mr. **Bramblett**. The question on fees for SBDC clients? May I address that?

Mr. **Mitchell**. Sure.

Mr. **Bramblett**. This is another matter that the folks at OMB have been raising. Certainly we agree that any small business that we assist should, in fact, return to the Federal Government what it takes from it, and I think in principle the small business community not only believes that, but does it. However, in terms of actually charging a fee for the program, I have reservations. If we are going to charge small businesses, single out 14.5 million firms, 60 million people then we need to single out other activities and Government programs and ask the agricultural community, and other folks which receive help to pay too. Obviously that is sacred and that is not going to be done. The point being made is that the small business community has been paying the bills for the Nation, and that can be proven. Now are we to ask for more?

We are here in light of a gigantic national Federal budget, penny-pinching a pitifully small program of $8.5 million annually, and at the same time we are asking folks that can't afford to pay fee charging professional consulting firms to pay us. We are nickel-and-diming this situation to death. That does not make sense to me. They will, in fact, pay if we do our job with assisting them by returning to this economy far more than they have taken out.

Mr. **Mitchell**. Based on the data you gave us this morning, the jobs created, the revenue from the business groups, that is more than enough payment, it would seem to me.

Mr. **Bramblett**. That is correct.

Mr. **Mitchell**. Good to see you again.

Mr. **Bramblett**. Good to see you, sir.

Mr. **Mitchell**. I will say in the dignified manner of a chairman, hang in there and keep slugging.

Mr. **Bramblett**. We will.

Mr. **Mitchell**. What I would like to do; I would like to hear from at least two more witnesses, and then we will take a quick break for lunch and then resume after that.

I would like to get Mr. Dan Moore, president of Image 7, a minority business firm.

TESTIMONY OF DAN MOORE, EXECUTIVE PRODUCER, IMAGE 7, INC.

Mr. MOORE. May I first say I want to express my appreciation for your concerns. I have been following what you have been doing over the past few years. I want to express our appreciation to you for taking the leadership in this very unpopular role.

Mr. MITCHELL. Thank you.

Mr. MOORE. I am with Image 7, which is a black-owned film company. I have problems with the word minority and what it does to me. It is a black-owned film company in Atlanta. We have been here for approximately 7 years. We can all agree that the success or failure of most small business is determined by many factors: Adequate capitalization, equity, skills of management, location, et cetera, but also the role of the Federal Government is significant in the success or failure of some small businesses. While I believe that the 8(a) program has great potential in concept, I think it has failed miserably in most instances to adequately help a lot of small businesses.

First of all, the redtape that is involved in getting into the 8(a) program is frustrating to most businesses, to say the least. We must also then deal with this catch-22. You are told by SBA when you find a requirement, we will certify you. Then you are told by all the businesses, all the Government agencies out there, that once you get certified, we will give you a contract.

Mr. MITCHELL. That is the most nonsensical mess that I have ever seen in my life. You keep our guys just bouncing back and forth over the net. With past administrators I have tried to press that point: Go ahead and certify the man. It almost seems to me that that is a deliberate means by which you prevent firms from becoming certified.

I won't interrupt you until you finish testifying.

Mr. MOORE. That is all right.

I think that is one of the problems that many firms have experienced—1- and 2-year delays in the 8(a) program—because of those requirements. I am recently the victim of losing a $1.5 million contract basically because the procuring agency, based in Mississippi, withdrew the contract because SBA failed to respond in a timely manner and also failed to request and initiate an impact study that was required. This is not uncommon in dealing with SBA. I have many other business persons and colleagues who have experienced similar kinds of problems, and the problem that I see with this is not only to hurt the small business person directly involved in this, but many of these agencies begin to take a very dim view of the 8(a) program, not because of the contractor, but because of their dealings with SBA or their failure to get things back to them in time. Many agencies are not even using the 8(a) program because they have had some bad experiences with the personnel at SBA.

In my particular industry, the Federal Government spends more than $500 million a year in audiovisuals, yet in the past 3 years, we have only managed to get less than $100,000 in contracts from these Federal agencies, despite extensive marketing programs to various agencies.

The problem of the 8(a) program lasting between 3 to 5 years, I think, is ludicrous. No business in this country can be asked to survive and become viable in 3 to 5 years. Until and unless small business persons are afforded the same kinds of considerations as our Nation's farmers, Chrysler, and Lockheed, likelihood of parity will never occur. We feel it is to the advantage of all of us not to try to establish new laws but to simply enforce those that already are on the books, perhaps establish an ombudsman committee that could oversee and monitor the activities of procuring agencies and SBA.

I am also convinced that the bottom line ends with the contracting officer in agencies who is at liberty to use the 8(a) program if he or she so desires, and is at liberty, for the most part, to get contracts into the hands of small businesses. I think these contracting officers have traditionally excluded small firms, and particularly black firms, and there are ways of writing regulations that will prohibit many small firms from participating in contracts.

Recently we submitted a contract, and were asked to give $3,000 with the contract. Many small firms cannot afford to post $3,000 just to bid on a contract. This was a requirement recently. It was a $1½ million contract and was a loss for us.

In conclusion, I feel there has to be something done with the contracting officers in the agencies, because the bottom line is: Everything that comes out of the agency comes through some contracting officer, and that person can do almost what they want to do with certain dollar volumes of contracts, to see they are awarded either to 8(a) firms, to small firms, or to their friends. Those are my comments.

[Mr. Moore's prepared statement follows:]

PREPARED STATEMENT OF DAN MOORE, EXECUTIVE PRODUCER, IMAGE 7, INC., ATLANTA, GA.

The success or failure of most small businesses is determined by many factors. Adequate capitalization, equity, skills of management, location, etc., all play major roles in the establishment and maintenance of a small business.

The federal government also plays a role in determining the success or failure of many small businesses. The 8(a) program has great potential in helping many disadvantaged businesses. However, there needs to be many major changes to make this program viable. First of all, most small businesspersons are frustrated by the redtape involved in becoming 8(a) certified. It has taken some firms more than a year to become certified. Other firms have been denied certification after spending a lot of time and money seeking to meet the criteria set forth by SBA.

We must deal with catch-22. The company is told by SBA they cannot be certified until they have filled out all the necessary paper work and found a requirement or potential contract. When the company calls on federal government agencies, seeking to obtain a set aside contract, the company is informed they must be certified first before they can receive a contract.

Many government agencies do not want to deal with the 8(a) program, not because of the 8(a) contractor, but because of bad experiences with SBA. The relationship between SBA and many federal agencies is strained, to say the least.

If the company manages to get certified, they must then go out and market their services. I am currently the victim of an 8(a) contract for 1.5 million dollars being withdrawn by a procuring agency because SBA failed to respond in a timely manner and request an impact study.

Such is not uncommon in dealing with SBA. The same holds true of advance payments and other requirements that place on the small businessperson grievous burdens and myriads of paper work that incumber progress.

Image 7 spent more than one year becoming certified. Despite the fact the federal government spends 500 million dollars a year in our industry, Image 7 has only received approximately 100 thousand dollars in contracts in the past three years.

To suggest that firms should only be in the 8(a) program 3 to 5 years is ludicrous. It is designed for failure and destined for business frustration. Until and unless the small businessperson is given the same considerations as the farmers, Chrysler, and Lockheed, the likelihood of parity will never occur.

It would be to the advantage of anyone seeking to improve the lot of small businesses not to establish new laws, but to see that the laws already in existence work. Perhaps Business Ombudsmen Committee needs to be created to oversee the procuring activities of federal agencies and monitor their program to assure equity in contracts for small and disadvantaged businesses.

Finally, it is my conclusion that the key to participation in federal contracts lies with the contract officer. This person determines which contracts will be offered to 8(a) contractors. Perhaps this person should be more closely monitored to assure fairness in the awarding of government contracts.

Mr. MITCHELL. Thank you.

What percent of your business at present or in the past has been with other than the Government? Are you doing business with the private sector?

Mr. MOORE. Yes, we are. Sixty percent.

Mr. MITCHELL. Therefore, it would be 40 percent with the Government, if you could get it?

Mr. MOORE. Right.

Mr. MITCHELL. I may have to hold you a little while, because I want you to walk the committee through the loss of this $1.5 million contract. When did you first learn about that contract, and how did you first learn about it?

Mr. MOORE. In May. I made a call to SBA and talked with someone there regarding Image 7 not having received many contracts through the 8(a) program.

Mr. MITCHELL. May 1981?

Mr. MOORE. Right. I was called back that same month. I was told there was a requirement of $500,000 a year for a contract in Columbus, Miss., at an Air Force base. We began at that time communicating with the Air Force base directly at the request of the person here to start negotiation. The contract was supposed to begin in September 1981. We were informed by the Air Force base there was some delay on SBA's part, so it was then being postponed until January 1982.

Mr. MITCHELL. Do you know what the nature of the delay was?

Mr. MOORE. I learned later they requested the SBA, back in July, to respond and had not received a response from 8(a) as late as July.

Mr. MITCHELL. That was 5 months; the contract was to begin in September?

Mr. MOORE. Right.

Mr. MITCHELL. In July, the Air Force tells you that in July they asked SBA to respond, right?

Mr. MOORE. Exactly.

Mr. MITCHELL. When were you told that?

Mr. MOORE. Not until November. I was only told this July that there was going to be some delays in the contract. It was going to be postponed until January 1.

Mr. MITCHELL. But the contract was to begin——

Mr. MOORE. September.

Mr. MITCHELL. September?

Mr. MOORE. Exactly.

Mr. MITCHELL. With what office of SBA were you dealing?

Mr. Moore. With the office here, with Sid Solomon, the representative of the office here.

Mr. Mitchell. In Atlanta?

Mr. Moore. Atlanta.

Mr. Mitchell. Go ahead with your story.

Mr. Moore. We made several trips to Mississippi to get the contract information in our hands. We submitted our contract to them at their request in October to begin in January. When I called Mississippi back in November to see the status of that particular contract, I was told then they had informed SBA 2 weeks ago that it had been withdrawn. I was never notified by SBA that it had been withdrawn until I contacted the SBA. They said to me matter-of-factly, yes, that is true; it was withdrawn about 2 weeks ago.

I looked into the reason it was withdrawn. It was withdrawn because SBA failed to do an impact study on the individual who currently had the contract. It was another small firm which had the contract out of Valdosta, Ga.

Mississippi then withdrew the contract. They said, No. 1, our budget was too high, based on figures from SBA; No. 2, they had not received word from SBA in time initially; No. 3, they said SBA had failed to do the impact study, and the person had filed a congressional protest. Based on that, they said it had to go up for competitive bidding in January. Then I was informed I would have to have $3,000 to submit with that proposal.

Mr. Mitchell. Is there anyone from the SBA that can give us some enlightenment on this $3,000 posting requirement?

Mr. Widemire. Mr. Chairman, I can only assume that that is a so-called bid bond; $3,000 sounds like an initial bid bond. Not a performance bond, but an initial bidding bond. That is what it sounds like.

Mr. Mitchell. Let me ask you——

Mr. Widemire. You can either post a bond or put up $3,000 cash. You get it back, though. I think it is a bond.

Mr. Mitchell. Yes, but even if you get it back, that is a heck of a lot of money to ask from a small business firm.

Mr. Widemire. I agree.

Mr. Mitchell. Let's dig into that a little bit, Major.

Mr. Widemire. It goes back to what the lady was saying earlier about the personnel service contract and her having to bond.

Mr. Mitchell. Let me ask you, you don't have to answer this: Could you give me an estimate as to how much money you spent in pursuit of this contract, you talked about several trips to Mississippi and so forth?

Mr. Moore. A ballpark figure would be $2,000 to $3,000, a ballpark figure. We devoted almost all of our time exclusively to this proposal, getting information from Mississippi, getting all the legal requirements, from a company in Mississippi. All the requirements for taxes, all the requirements for everything that we would have to do in Mississippi, getting subcontractors to perform for us, personnel to perform for us, advertising in a local newspaper there to acquire staff. We did all of those things based on——

Mr. Mitchell. Somewhere between $2,000 and $3,000 was spent in pursuit of that?

Mr. Moore. Easily. That is a modest figure.

Mr. **Mitchell**. This is almost a rhetorical question: Would you have done that without the encouragement of SBA or without the encouragement of this Air Force unit down in Mississippi?

Mr. **Moore**. I would have incurred some expenses if I thought the contract was indeed $500,000. I am learning now from Mississippi the contract was only for $150,000 a year.

Mr. **Mitchell**. Who told you the $500,000?

Mr. **Moore**. SBA.

Mr. **Mitchell**. Who in SBA?

Mr. **Moore**. Sid Solomon in SBA, which is a figure someone gave him from the Air Force base in Mississippi. I would not have pursued that contract for that kind of money because of what they wanted done, for that dollar amount.

But I guess what I am saying, also, is that I doubt seriously if the Air Force base would use an 8(a) program again because of what they encountered in terms of the delays, in terms of the frustrations on their part, in getting SBA to respond to them in a timely manner and to get a proposal submitted.

I think what happens is many of the agencies are turned off by dealing not with the contractor but with SBA.

Mr. **Mitchell**. Mr. Regional Administrator, I don't like to impose burdens on anyone, but would you just track this one through for me?

Mr. **Widemire**. Yes, sir. I have partially tracked it, Mr. Chairman, already. Of course, it was a requirements contract, and, as you are probably familiar, in Government procurement you say we have an annual potential requirement of $500,000. That does not mean we are going to have that much, but we may have that much. Experience had shown a couple of years it had run about——

Mr. **Mitchell**. Somewhere along the line, someone knew it would not be $500,000.

Mr. **Widemire**. The procuring activity possibly had some idea. Maybe Mr. Moore did not understand the use of the term requirement. When it said it was a $500,000 requirement.

Mr. **Moore**. I have it in writing.

Mr. **Mitchell**. Again, let me try it another way.

This committee would really appreciate a detailed account of this contract.

Mr. **Widemire**. Shall do, sir.

Mr. **Mitchell**. From inception to collapse.

I would just have to assume that Mr. Moore has been in business for 4 years——

Mr. **Moore**. Seven years.

Mr. **Mitchell**. Seven years, rather; that he knows the terminology associated with doing this. I would have to make that kind of assumption.

I would also like to be able to assume that the SBA officials here, somewhere down the line, would have picked up the exact amount of that contract that was really going to be let and would have notified him.

The reason I want a full report; it just looks like kind of a loose operation to me. That is unfair of me to judge based just on your testimony. It certainly suggests to me there was not the kind of tight working relationship with this gentleman as there should have been.

Mr. **Widemire.** I believe that would be a fair assessment; not overly stated.

Mr. **Mitchell.** Would you try to get that resolved as quickly as possible?

Mr. **Widemire.** I would just like to call to the attention the impact study was done. The impact study indicated that under the rules and regulations, we could not have subcontracted it to Mr. Moore.

Mr. **Moore.** When was it done? November?

Mr. **Widemire.** I can't give you the date.

Mr. **Moore.** It was done after the fact.

Mr. **Mitchell.** If I may, please, gentlemen, I think I would like to get that full, detailed scenario date-by-date, name-by-name, step-by-step. I would like to get the same thing from you. I want to compare them. Something is wrong when you get this kind of situation developing.

Mr. **Moore.** The impact study was done after November. Correspondence from the Air Force base in Mississippi indicated to me they had alerted SBA back in July that it would be extended if they did not respond within 10 days.

Mr. **Mitchell.** Will you get me your step-by-step, date-by-date, name-by-name progress on this report? And I would like to compare these two. Something has gone wrong. There is no escaping that.

Mr. **Widemire.** We are delighted, though. We understand Mr. Moore is going to competitively bid, so we are delighted with that.

Mr. **Moore.** They asked for a $3,000 cash deposit. So I can't competitively bid. There is no way.

Mr. **Mitchell.** Even if you could competitively bid, that would be delightful, but that still does not solve a problem that I see before me in this case. You are talking about May of 1981, running all the way through until November without any finalization and with really not the capability on the part of either the Air Force or SBA or somebody to finalize it. That is just a bad process.

Thank you, sir.

Mr. **Moore.** Thank you.

Mr. **Mitchell.** Our next witness is Mr. Ayodele Shedeke, the International Shared Services.

TESTIMONY OF AYODELE SHEDEKE, INTERNATIONAL SHARED SERVICES, INC., ACCOMPANIED BY GLENN ERIC STAMPS

Mr. **Shedeke.** I am originally from Africa. I was born in the West Indies and have been in the United States for the last 13 to 14 years.

Mr. Chairman, Mr. Clark, minority counsel, we thank you for this opportunity to testify before this committee.

I originally intended to read from the statement, but we have opted more or less to tell this committee some of the things that have happened to us very recently, some of the experiences we as black businessmen experienced, specifically in the local market.

We can come here again and reiterate the problems that minorities and blacks are experiencing in acquiring capital. The requirements for track records, the requirements for collateral, we can tell you about the experiences that we have had in the restricted market, but we prefer to give you some specific examples without citing any companies or names.

We would like to also speak from the point of view, of course, we are a brandnew business. We are only 5 months old. I guess that gives us a unique perspective on things. It gives us a perspective that most of the other businessmen may have forgotten; I don't know. For example, we sit here and hear the Small Business Administration officials say good things about themselves. I hope most of it is true, because we will give it a try sometime soon and see if this thing really works.

Unfortunately, though, we have opted not to even go that route as yet, because for every one good success story we hear about SBA, we hear 10 or 15 horror stories. We, as new businessmen, believe it is essential to put our efforts in the productive capacity of business and to try to produce rather than go to the wall with the redtape and bureaucracy that we know is waiting out there for this business. We have made a commitment; six minority persons have made a commitment to engage in a new way of life, in effect. That is, we would like to be allowed to be productive, not just merely consumers within the American economy, but part of its productive capacity.

I will tell you about the fact we have had problems trying to secure capital. We secured some capital based on the fact that I had a personal acquaintance with a——

Mr. MITCHELL. May I interrupt you just a minute? What is your service or product that you offer?

Mr. SHEDEKE. International Shared Services—reading from the testimony now—is a combined effort of eight persons, three women and five men. By the way, we are up to 11 persons now. We hope to provide as our business expands an array of financial, accounting, and other services. Presently our operations range from the collections of delinquent commercial debts to the total management of accounts receivable.

Mr. MITCHELL. OK.

Mr. SHEDEKE. We have a wide array of services that we try to present to other businesses. We have recently embarked on some measure of diversification. That is, we are hoping to go into our community and give H&R Block, and Mr. Tax, and these other people a fight for their money. The market is there. This is our local market. We think we should penetrate that market. However, I was beginning to explain the fact that the acquisition of capital for any small business is specifically difficult if you don't have any, "connections."

You know, one of our principals applied for a $5,000 loan in a community bank within our community. He could not get it. I would daresay that had that loan been applied for to purchase an automobile or some item of furniture, it would be easily acquired. I think the general attitude among the banking industry, especially in the black communities, is really not to reinvest any type of substantial capital within that community.

We have experienced this within our own community as far as the capital acquisition is concerned, and as far as access to the market is concerned. To be specific, we have, as I mentioned, started a tax service that we think is quite competent and can do as well as, if not better than, some of the national firms. However, to do this in a very effective way, we need access to the market—our community.

Well, my associate and I here approached the management of South DeKalb Mall and asked them very politely what we would have to do to set up some kind of booth within their mall to sell services to the public. Their response was, of course, after going through a lot of runaround, that they had enough tax services. Of course, we know that. The first question that came to my mind was, what happened to the good old American system of free enterprise? They have decided there was enough.

Of course, we don't subscribe to that view. We believe that we are being kept out of the market because we are competitors, competitors that probably will perform well and capture some of the market that H&R Block, Mr. Tax, Sears, and K-Mart and those other stores currently have.

Of course, we are not going to let it rest there. We have decided that we can do some things to get their attention. If I might digress a little, one time we had a fight, for lack of a better word, to get to this point. We had to struggle to get to the point where a simple thing such as voting was allowed. We also had that fight in the educational sphere.

I think now the fight or the struggle we have on hand is an economic one. I think that most of the minority population in this country, realizing that we are 30 million people in this country, have started to become restless again because of the fact that we at this point want to participate in an economic system that we believe we should be allowed to participate in.

How do you do this? Well, you do this by venturing out and starting small businesses. I don't think any business, unless there is an excessive amount of working capital, can start off big. We all start off with a very small scale, as I think Congressman Gingrich said. We are in our infancy stage. We realize this, of course, and will proceed accordingly. However, the obstacles that are there, the obstacles that are placed there intentionally to preclude small businesses, not necessarily only black or minority businesses, but to preclude small businesses from the marketplace, have to be dealt with.

We have started to use some, I guess, unorthodox ways in doing this. We have started to elicit the support of our local community. After all, they are the ones that we are catering to at the present time. We, also, of course, have to address the issue when we go to a company like Southern Bell, that has 80 percent of the local market as far as minority consumers are concerned, but if you look at the record at what portion of their business is being done with other minority businesses, you will find it is a very miserable one. Those things have to be addressed.

I guess I have quite a lot to say, and I am sure Mr. Stamps has a lot to tell you, too. I find myself in the predicament of having so much to say that I don't know which should take priority. One thing, additionally, that I would like to say as far as small businesses are concerned, is that established businesses, and America as a whole, should not feel threatened by small businesses, because the only thing that small businesses in effect will do is allow the total resources of this country to be utilized.

We have resources yet untapped; we have personal resources; we have human resources out there that can be utilized to allow this country to become more competitive and to produce more. If you would take a look at the international scenario as far as our productive capacity and our ability to compete is concerned, you would find that we are losing ground. We are losing ground to the Japanese. We are losing ground to some other Third World nations that are just coming into the picture.

If this country were to use all of its productive capacity—and by that I mean allowing small businesses their assistance, and giving them the assistance to set up as a small business and produce the services and products that they can bring into the marketplace—you would find that this country might indeed become more competitive again and have a better access to the Third World countries as far as using all its personal resources are concerned.

For a specific example again, talking about the total utilization of this country's resources, what we have experienced in the last 5 months has been encouraging and at the same time frightening. We have effectively created 11 new jobs in 5 months because we decided to do something different. We all came from relatively stable and secure jobs, but we realize there is a very important aspect of this Nation's economy missing and that is the participation of minority and all-black businesses.

You know, we are supposed to have 30-odd million people in this country and therefore have a vast market.

We are supposed to spend approximately $140 billion a year and therefore we have a very important aspect or a very important part of this country's capital. However, none of it is ever kept to any great degree within the black business structure or the black community.

I think these problems are very basic to the failure of black businesses and minority businesses. Let us face it. If the market is not open to a business, I don't care how good your personnel are I don't care how good your product is, if you don't have the market available, then you are going to fail.

There are some examples that I can cite. For instance, M. & M. products here in Atlanta. They encroached, if I might say so, on a market that was there, but a market that was more accessible to a black business because they manufactured black products, black hair products.

Look at the tremendous success. That business was allowed to or could capture part of the market. That is by example. You would find the same thing goes as far as the international market is concerned. If, for some reason, the United States had a problem with penetrating the Latin American market, for example, and you can have a business that represented those people's aspirations, represented their hopes and had their interest at heart to infiltrate and penetrate that market, not only would it benefit the local economy, the local business or the black business and concern, but also the total economy of the United States.

I think we need to start looking at the development of minority-owned and black businesses from that prospect, not only on the local level, but on an international level. Let us face it, these Third World countries are becoming more and more sophisticated. They realize there are 30 million black persons in this country, but they see no meaningful participation when businessmen from their countries or from this, our country, interchange ideas, go to conventions, and there aren't any minority businesses to represent, these countries do and will tend to turn to other sources for their goods and services, and that has happened, as a matter of fact.

I am sure Mr. Stamps has a few things to add if you have no questions for me at this point.

Mr. MITCHELL. I would like to hear from him first and then come back to you.

[Mr. Shedeke's prepared statement follows:]

PREPARED STATEMENT OF AYODELE SHEDEKE, INTERNATIONAL SHARED SERVICES, INC., DECATUR, GA.

We would like to take this opportunity to thank your subcommittee for the invitation extended to us to discuss some of the problems encountered by small minority businesses. International Shared Services, Incorporated (I.S.S.I.) was incorporated in August of this year. Although we are a fledging business, we have had an opportunity to suffer some of the frustrations and to experience some of the rewards in the operation of a small business.

I.S.S.I. is a combined effort of eight persons: three (3) women and five (5) men, who are providing and who hope to provide, as our business expands, an array of financial, accounting, and other services. Presently, our operations range from the collection of delinquent commercial debts to the total management of accounts receivable. Although we are aware of some grim difficulties which befall minority-owned businesses, we do foresee excellent opportunities for the regional and international growth of small minority organizations in the United States.

During our short period of existence, we have noticed serious hindrances to the creation and development of small minority businesses. A description of some of these obstacles applies to all small businesses in general, but a significant number of these problems are distinctly peculiar to minority-owned businesses. We have experienced the following difficulties in our business operations, and we hope that a disclosure of these problems will assist you in helping minority-owned businesses generally with effective solutions.

The problems concerning the development of small minority-owned businesses may be divided into at least three (3) main categories: (1) the strangulation of the flow of capital; (2) the existence of entrenched biases against minority persons in business regarding the latters' abilities to create and execute complex and simple economic strategies to deliver goods, products and services at competitive and attractive prices; and (3) the lack of a central repository of information about laws, programs, and other sources of knowledge to assist the small business person.

First, the closed market practices of banks and other established businesses stand as pre-eminent obstacles to the development of minority-owned businesses. We have experienced the perplexing problem of attempting to satisfy established businesses' insistence upon the demonstration of a "track record" despite our relatively recent origin. The attempts to place this burden of proven excellence or accomplishments upon minority-owned businesses, effectively precludes the reluctant newcomer from any opportunity to compete and to advance. For example, just recently a bank resisted our requests for two types of operating accounts because of our presumed inexperience and unprovenness. Moreover, on a more general note, we are all aware of the practice of banks to insist upon personal collateral and indebtedness to secure even relatively modest loans as a source of capital, but not upon the provision that past accomplishments must be demonstrated. Our relationship with potential clients, with lending institutions, and sadly as explained below, with our fellow minority entrepreneurs bespeaks the minority business person's inability to pierce the business and social network which recirculates capital and influence among the established ingroup. The restrictive practices of the lending institutions are extremely damaging because loans constitute the major, if not the only, source for the creation and expansion of minority-owned businesses. The sale of stock or the issuance of bonds to raise capital is an unrealistic approach for the solution of our problems.

Such restrictive practices may or may not have had a legitimate purpose when initially created, but they have outlived their utility in the modern economic setting; these practices have also created added and unnecessary burdens to the development of small businesses which cannot contain their requirements and needs within such rigid frameworks.

We feel that established businesses, once again, are unfairly favored at the expense of small minority-owned businesses which merely desire an opportunity to compete in the free forces of the marketplace.

A second serious problem which faces minority businesses is the mistrust and hostility toward the creation and development of these businesses. Ironically, stereotypical attitudes among established businesses about the alleged pervasive incompetence; lack of sophistication; and ignorance of small minority-owned businesses have encouraged the very business failures and economic distresses which plague the Black communities of this country. For example, in years past, Black business persons benefited from the albeit odious practice of de jure segregation, because consumers were forced to patronize accordingly. In recent years, however, integration has flowed in one direction only allowing Blacks to patronize white businesses while blocking Black access to both the White and Black markets.

We were recently told by a prospective client that the utilization of our services presented a "sensitive" problem in view of that concern's unwillingness to experiment with a new minority-owned business. A significant business opportunity was lost for us because the prospective client refused to patronize our services and to develop a mutually beneficial relationship.

We sensed that there was a lack of confidence held by this prospective client in our ability to achieve results without causing problems stemming from our status as minority entrepreneurs; we sensed that there was a reluctance to consider our operation as an opportunity for that prospective client rather than an unhealthy risk. The shame and pity of such an attitude is highlighted by the fact that we are providing the same type of services to another client in question. Obviously, the success of our business, at least in its initial stages, will depend upon the extent to which established businesses can appreciate the need for reciprocity, mutual aid and protection.

Nor are we blind to the rather obvious fact that established businesses, which have a vested interest in restricting competition with their panoply of political and economic influences, have helped to disseminate certain stereotypes about minority businesses and to create obstacles to ensure our failures. We can expect no less from established competitors or their clients but we are dismayed to sometimes meet such attitudes on the rebound from our fellow minority entrepreneurs with whom we seek, whether as clients or as competitors, a true partnership and sharing of resources. For example, we may have an opportunity to market a line of products or services in a joint venture relationship with another corporation which intends to market the same line. But there is no need for competition here when, by working together, we can maximize our respective resources, knowledge of the industry, and business relationships to expand the market to suit our dual interests.

And lastly, small minority businesses would be greatly benefited by the easy availability of a storehouse of information which would assist small businesses with the development of a business or any phase of it. The lack of a reliable means to locate qualified, eager, and capable employees (a factor so crucial to a new business), for example, has been as much of a problem in business as has been the lack of capital to pay such employees their salaries. At present, only two (2) of the eight persons in our organization are getting paid salaries, and the rest of us are enduring financial hardships because of our as yet limited resources and willingness to sacrifice. Too often prospective minority-owned businesses are forced to solicit the advice of those who have already failed in their business or who have never attempted the challenge of self-employment itself, resulting in disastrous consequences. Acutely aware of our own recent endeavors, we seek advice even from those who lack proven "track records." We need a reliable, comprehensive body of information to guide us in our efforts.

Access to capital and to the information which would assist us in prudent long-range planning would be of great assistance to minority-owned businesses. Minority entrepreneurs today are frequently sophisticated, educated, and industrious professionals who simply lack the capital and some specialized knowledge about the operation of a business to realize their aspirations.

We suggest that the following steps if taken might alleviate some of our problems:

(1) Minimum wage requirements should be re-examined in order to address the problem of a 46 percent plus, unemployment rate among Black teenagers. We have a surplus of labor and if such labor costs can be reduced, then the development of labor intensive industries should address both the unemployment problem, as well as the lack of minority participation in commerce generally;

(2) Joint-venture capitalism should offer true incentives (perhaps tax credits or other inducements) to established businesses by pairing them with minority-owned businesses; all too frequently, joint-venturism has produced an anemic relationship between a marginal white business and an unhealthy or a totally new Black business, thereby insuring the failure of both businesses. We propose a joint-venture relationship so that minority-owned businesses would capture that part of the market which established businesses may have access to but which they have avoided, rejected, or simply failed to develop.

(3) The availability of capital, as always, presents a constant problem and could be addressed by:

(a) The exertion of political pressures to encourage the executive branch of government to implement mandated levels of minority participation in local public works projects;

(b) The creation of joint-ventures between minority-owned businesses in the U.S. and businesses in the Caribbean and in other Third World countries, stimulated by the availability of markets in these foreign countries for foreign goods. In this respect, minority persons in this country who are politically influential can serve as a valuable link between minority-owned businesses here and the developing industries in the Third World countries.

If minority-owned businesses have equal access to all types of markets, there will be little, if any, problems to plague the development of Black businesses. Conversely, as long as minority-owned businesses here are totally geared to Black consumers and are shut off from exposure to other markets, minority-owned businesses will remain at a distinct competitive disadvantage in comparison with established businesses on a national and international level.

The lack of confidence within the minority communities about the competence and capabilities of minority entrepreneurs will probably diminish as these businesses succeed and offer concrete, proven examples of accomplishments. As we succeed, we will address not only the particular problems of minority-owned businesses, but also the general sense of despair and hopelessness which accompanies high unemployment; wasted and unused talents; and a belief in false stereotyped attitudes.

We believe that your subcommittee has an excellent opportunity to formulate and sponsor legislation to combat these problems which we have discussed. When given an opportunity, minority-owned businesses will prove to be the effective means of reducing governmental involvement as a panacea for the correction of social ills. Moreover, such businesses will spur competition and revitalize the American tradition of affordable excellence in goods and services.

We must caution this committee and all others, however, that the minority-owned businesses of today are decidedly different from their counterparts of the 1960's. Although we are products of the 1960's, we are not wedded to any ideological dogmas which would obstruct the main goal of creating successful and financially lucrative institutions. Nor are we impressed by puffery; inflated egos; and facades which create the illusion of success and accomplishment. We respect hard work, expertise, and solid achievements.

It is the firm conviction of I.S.S.I. and, we hope of other minority-owned businesses, that we will accomplish our objectives irrespective of the obstacles placed before us and without any regard for the lack of cooperation by those who can but are too unwilling or too timid to help us.

Mr. STAMPS. Mr. Chairman, those here in attendance, there is one light comment that I would like to make in making note of the comments made previous to our particular testimony, and that is if more small businesses were to turn to farming, perhaps we wouldn't have the problems that are now being experienced.

Mr. MITCHELL. You ought to hear the farmers when they come in.

Mr. STAMPS. On a more serious note, I would like to mirror my concerns regarding the plight of small businesses, but more particularly those experienced by black-owned and operated firms.

We are a corporation that provides management services not only to the private sector, but also with some hope that in the future we can provide these services to the government because they are very useful services that are in high demand.

The need for competent fiscal management, particularly with the economic trends as they are today, become evermore apparent. These services obviously cannot be provided by any less than highly skilled and qualified individuals.

The president of the firm, Mr. Ayodele Shedeke to my right, is a very experienced accountant, a former comptroller with a hospital authority in a county of Georgia. His experience alone bespeaks the other combined experience of those who have formed International Shared Services.

Our problems are one in that a service which we provide has formerly not been offered by a minority-owned firm. That means that we are going out into the market, approaching people who have not been accustomed to the type of skill and technology that our firm possesses.

This has hindered our efforts considerably in terms of obtaining contracts or in terms of having various different roadblocks placed upon us which, we, after researching and having our legal counsel look into are quite unfair and quite biased.

To cite examples, the subject of bonding—and it is my understanding, Mr. Mitchell, that you had questioned whether or not management firms or consulting companies were required to have bonds in order to engage in business practice; and to answer your question, quite frankly, yes, it is a large problem that our firm has experienced from its inception.

Several of our contracts are with colleges and universities whereby we handle the collection of defaulted student loans. These are Federal loans that are assigned by the Department of Health, Education, and Welfare on student insured student loans, health profession loans, national student defense, and national student direct, loans, to name a few of the types of loans we service through institutions that are now under contract with us.

However, in many instances the colleges seem quite willing to enter into contracts with us, but at the bottom line we are asked to provide a bond.

In trying to satisfy that bonding requirement, we have gone to the various different insurance companies or bonding agencies and we have completed applications, gone through the routine procedures, and have been told that unless we have 2 years of financial statements to provide or unless we have a "track record," that this is not a practice that bonding companies are now doing.

They are not providing bonds or this type of insurance indemnification for young or small businesses.

Needless to say, it precludes us from the opportunity of engaging in several contracts. In many cases we have lost contracts or we have had contracts held up because of the lack of bonding requirements that the company doesn't have.

I don't think that the question so much is in having these services available to us. I think that more of the concern lies in the fact that first of all the understanding of a prospect or prospective client, might I say, in understanding that, No. 1, in order to get established you must develop; you must have someone to place the trust and confidence in your own ability to perform based upon the willingness and acceptance of one's ability through a demonstrated performance under a contract.

At that particular point you begin to develop a track record.

I think it is quite preposterous to consider that a company that is 5 months young should have 2 years of financial statements or any criteria which is so high that it is unobtainable or it is inaccessible to their growth and to their development.

These are some of the types of problems that we have. They are far reaching in scope in that not only does it eat away from the incentive and the initiative that is needed during the early growth and development of a new business, it also is very discouraging. When you are going through all the steps to make sure that your i's are dotted and your t's are crossed and that you have your legal wherewithal in front of you, but yet you are hit with one burden after the next, the subject of bonding is only one clear concern that we can demonstrate.

The others are the lack of participation of large corporations in the private sector and in the government to be able to provide a mechanism whereby the release or flow of information is available to let minority businesses know what jobs are open and available for bidding.

In many cases I find out myself because being in direct control or in direct charge of the marketing and sales for our company, I have to take the initiative to find out what is going on and where it is going on.

If I did not assert myself or make known this information through the other members of the corporation, we would not know.

For example, there is the consortium agreement in Washington, D.C. for educational services that are provided to colleges and universities nationally.

That consortium agreement is between the APOA——

Mr. MITCHELL. What is that?

Mr. STAMPS. The APOA is the Alliance of Personnel Officers and Administrators. They somewhat set upon a college curriculum. This is NASFAA, the National Association of Student Financial Aid Administrators, and the National Association of Business Officers and College Officers.

These three associations provide basically the same three types of services that our firm offers. There was a contract recently signed. Needless to say, the amount of that contract was not disclosed, has not been made known to me, but it was of considerable size. It was for a 3-year period of time.

It was signed by the Federal Government through the Department of Health, Education and Welfare or SLEMA, two of those groups combined whereby those organizations were to provide, and are providing, financial aid workshops and seminars, consultation and training, financial management assistance and other types of advisory services to colleges and universities whereby the Government cannot keep up with these things, therefore they give these work assignments to the consortium in order to carry out the workload.

We in turn found out about it on the shoestring or on the tail end, you might as well say, that this contract had already been signed but that as far as a public bid going out, that very little was known about it.

Actually I found out through Jack Reynolds at the Department of Health, Education and Welfare; that is the only way I would have known myself.

These are examples, examples such as the large corporations, Delta Airlines, Republic Airlines, Southern Bell, the Bell Phone System, needless to say, of which 40, if not 60 percent of all minorities are reliant upon phone communication.

Well, you have to say 100 percent of all minorities as well as almost any people in any ethnic strata are relying upon telecommunication as a means to keep in touch or for emergencies or whatever it might be are relying upon, our consumers are relying upon the corporations for flying or whatever it may be.

Yet if you were to look into the records again, as Mr. Shedeke stated, and determine how many of those large corporations do business with qualified minority companies, you would find it to be a quite disgustingly low percentage.

I think that in many cases there is a disheartened feeling by minority firms to continually voice their particular feelings regarding matters which in many cases are swept under the carpet after conferences like today's meeting.

I think that it bespeaks of a particular problem which the Government or its branches has not really faced head-on.

The problem is one that gives the people the opportunity to work and you will find less opportunity for high unemployment.

You will find less a need for welfare. You will find less a need for people to be categorized as indigent if given the opportunity to use the resources made available by Government without the redtape.

I think also that it is somewhat disheartening that a situation such as today's meeting where minority firms have had an opportunity to be present and air their concerns are unable to represent themselves in many cases because of mere survival.

Mr. MITCHELL. What do you mean by that? Why aren't they able to represent themselves?

Mr. STAMPS. I believe in many cases where you take the firms who have not shown today or that are not present merely cannot afford to take this valuable time out.

Mr. MITCHELL. Oh, OK.

Mr. STAMPS. In order to do so. We sat here this morning thinking about the dollars being lost while we sit here to state a cause or state a concern that perhaps again may be shoved under the carpet and not really looked at face value.

Mr. MITCHELL. Let me interrupt you at that point. I didn't say anything before, but now I am going to resent it. I don't shove anything under the rug. I think my record in Washington shows that.

I dig and probe and don't sweep things under the rug. I don't want to give the impression this is a pro forma hearing for things to be swept under the rug.

Mr. STAMPS. Again, Mr. Mitchell, don't misunderstand what I am saying. When I speak of the Government, I am speaking as a whole, not you or what you have done. It is apparent you have concerns and you have voiced them. I think we have great respect for you. Your track record is excellent.

It is not any personal affront to you or the Small Business Committee. We are merely speaking of a concern that is more widespread.

I think that this is again something that cannot be ignored.

Our feelings are such that if it takes anything less than a violent action and according to the way the economy is eroding right now, and according to the high feelings and sentiments that black people, the frustration that black people feel today because of having nowhere to turn is really looked at and we plan some actions that can be taken, the only result will be again—and perhaps more effectively—boycotting services that were—these things done during the sixties.

For example, during King's day, during the time when if a corporation did not cooperate, then you would stop using services. If black consumers would merely stop buying until they were equally represented in terms of the contracts being awarded, perhaps this would alert that there is a particular problem and that perhaps it would solve some of the ills of not only Government, but of society.

My closing statement is merely the track records, the financial statements, the accessibility to markets all boil down to giving a person their fair share. I don't think that it is anything short of asking for an equal chance in this economy and it is a desire of our firm to be able to voice these concerns in public, to be able to continue a struggle that we realize didn't start with the inception of International Shared Services, but certainly that we have a part in being able to perpetrate the growth of not only our firm, but also the survival of those that are in existence and also those who have a desire to motivate them to become entrepreneurs.

Thank you for giving me the floor.

Mr. **Mitchell**. I thank you for your statement.

I would add there is no philosophical difference between us, I don't think. I have not hesitated to say publicly throughout the years, and I will say it again in this hearing, I do not rely on the legislative process solely to advance the cause of blacks or other minorities. I think that would be foolish.

I do not rely solely on the courts to do it. I have been a part of and will continue to be a part of certain activities and techniques that I think are required to move us toward economic parity.

When you decided to go into this business, did you figure out your capitalization operating under the old time-worn theory first year you lose money, second year you break even, third year you might make a profit?

That is the general axiomatic statement.

Did you plan capital to get you through your first year?

Mr. **Shedeke**. Yes. I did some projected cashflow analyses as to what was required. If you again look at the total requirement and what will actually keep a business in business without making the sacrifices that we are making, you would find that that kind of capital acquisition is almost nonexistent.

For an example, we have been in business for 5 months, thereabouts, approximately 5 months. I think the 27th of this month would be 5 months.

Six of the principals have not drawn any salaries or wages since that time. We are going solely on what we have personally been able to secure as far as our working wives are concerned.

Again, we are making some sacrifices in place of the capital that is not available. We are also trying to come up with some innovations as far as bonding requirements are concerned.

We are coming up with some new ideas that, if applied, can work, some of which I won't discuss here.

But yes, we did do some capital cashflow projections and I might add that if we did this totally by the book, we wouldn't be in business.

Mr. MITCHELL. You are not prepared to deal with SBA at the present time. You want to get a more sound footing, but it is clear that you could use some assistance from some source. That is very evident.

I commend you for your own efforts in plugging away at trying to break into it.

Is there something like a minority purchasing council which might be of assistance to you or some entity of that sort?

Mr. SHEDEKE. There is a minority purchasing council, I think, here in Atlanta for this region. Again we realize there are many things we should be involved in.

Mr. MITCHELL. Have you been in contact with them at all? With the minority purchasing——

Mr. STAMPS. To some very small degree. The chairman of the Atlanta Regional Minority Purchasing Council and I are personal acquaintances to some degree.

Again our biggest problem is being slowed down, I think, more than anything else. If we could get the contracts in hand, if it wasn't tied up with so much process, we would find the business——

Mr. MITCHELL. Not all of these purchasing councils work uniformly or equally as well, but I have some personal knowledge of some of the councils that we have in the country. Remember, most of them that I know of are made up of members of the private sector. That is their job, to get the business for you. That is their objective.

It has been my experience with one or two of them that this is done with minimal redtape because the private sector, like everybody else, doesn't want a whole lot of redtape. I am certainly not offering that as a panacea, but it seems to me if you want to try to break into the private sector, you go to that group which is made up of the private sector and at least enter into an exploration dialog with them to see what, if anything, can be done on your behalf.

I don't know of any other recommendations that I can make to help you out right now, but I think it was important that your statement be incorporated into this record.

Mr. Bramblett, did you hear this testimony?

Mr. BRAMBLETT. Yes, I did.

Mr. MITCHELL. Can you be of any help?

Mr. BRAMBLETT. I might be.

Mr. MITCHELL. Would you get together with him?

Mr. STAMPS. Sure.

Mr. MITCHELL. It is rough. It is extremely tough. Don't quit. One of the first firms that I had contact with when I first went to Washington got its SBA loan of I think $100,000, which was a miracle during those days. Most loans were $37,000. That firm grossed $14 million last year, so it can be done.

The guy's hair has turned as white as mine. He is irascible and almost as cantankerous as I am, but he succeeded. So I am just giving you that little word of encouragement.

Mr. SHEDEKE. For $14 million gross, I will give up my hair.

We thank you for taking time out to listen to us and for the interest you have displayed in minority business. Please realize we came to this hearing with a lot of frustrations because we go back out there into the real world and we have to deal with them.

Mr. MITCHELL. Sure.

Let me tell you gentlemen, you haven't had any frustrations until you try to deal with a Congress that has no commitment to minority business. I share your frustrations.

We only have one more witness. It is 1 o'clock. I was wondering if you want to take a 5-minute break and we will hear the last witness.

I know a number of people canceled because of problems with heating and so forth.

Why don't we take a 5-minute stretch and come to you, Ms. Smith?

Let's take a 5-minute recess.

[Recess.]

Mr. MITCHELL. I would like the hearing to resume now with one announcement.

When we conclude this first section, I am advised there are four other witnesses who want to appear and we will try to resume at about 2:00 or 2:15 and wait for those witnesses to show.

Ms. Smith, if you will come forth now and give your testimony.

TESTIMONY OF LINDA A. SMITH, PRESIDENT, L & L ELECTRICAL SERVICES, INC.

Ms. SMITH. Thank you, Mr. Chairman.

I could kind of shorten my testimony by saying if you double everything that was said today, you would have the woman's point of view.

Mr. MITCHELL. Now, will you pull your mike a little closer to you?

Ms. SMITH. However, I very seldom give my opinion except when it is to my advantage.

What do the names Rockefeller, Carnegie, Mellon, have in common with 7.1 percent of the population?

The fact that they are all entrepreneurs, but this is the only similarity. For that 7.1 percent represents the total number of women entrepreneurs in our country in 1977.

I am honored to have been selected to present this testimony on the problems attendant with women entrepreneurs entering the business sector of the economy because I am at the very pulse of the problem; I am most sensitive to its meaning and implications.

Therefore, my testimony will address the basic statistical data on women entrepreneurs, my own personal experience and some recommendations for the resolution of the problems faced by women as entrepreneurs.

Long before President Carter issued Executive Order 12138, creating a national women's business enterprise policy of affirmative action to aid women-owned business, those of us who happen to be women were already fully convinced that the various business opportunities in this country should be available to us on an unbiased basis.

Even with an Executive order, it will be only those women and other minorities who are bold enough to brave what was long regarded as a masculine institution that will move forward and survive.

While women constitute more than half of this country's total population, the Bureau of Census statistics in 1977 revealed that only 702,000 of the Nation's businesses were owned by women.

These businesses had revenues of $41.5 billion, or 6.6 percent of all receipts for the year.

Further description of these women-owned businesses reveal that most of them were classified as small business, and half of them were operated from residences. More than 70 percent of them had only one full- or part-time employee.

Also, women business owners were likely to be first-time entrepreneurs, with a median of 15 years as paid business employees, and 7 years as managers.

As a woman who started a corporation with $1,000 and worked as a file clerk, secretary, bookkeeper, financial analyst, personnel manager, on the clerical side, as a project manager, estimator, electrician's helper, and truck driver on the semiskilled labor side, and now, as a woman who is the major stockholder, chief executive officer, and chairman of the board of that corporation, I feel well qualified to speak accurately on the problems facing women entrepreneurs.

One of the major problems facing women entrepreneurs is alleviating the bureaucratic mazes. Constantly we hear promises from government that certain regulations that are unnecessary will be lifted, as well as other administrative barriers; yet the female entrepreneur has begun to recognize these promises as only lipservice.

Second, there needs to be a mechanism to insure that women entrepreneurs receive their fair share of governmental purchases, contracts, and subcontracts, as well as their fair share of the sale of governmental properties.

Third, and perhaps the greatest problem of all is the establishment of credit to meet initial capitalization requirements of our businesses.

In 1976, when I assumed the position of president of L. & L. Electrical Service, Inc., we were just entering a joint venture arrangement to perform a contract that was at that time worth $9 million. Today this contract, still incomplete, is at a price of $13 million.

Prior to this involvement, our company was unable, even with an SBA guarantee, to get a loan of $25,000. However, after entering the joint venture contract and getting a commitment from our majority partners to guarantee the loan, we received the loan.

We then proceeded to process smaller contracts while continuing our participation in the joint venture project.

Because we were now being approached by various governmental funded agencies who wanted to claim fame for the procurement of this $9 million joint venture contract, we were then offered various types of assistance.

Thus we bid on another contract in the amount of $396,000 which still was extremely large for a company that could only borrow $25,000. Nevertheless, we were assured by one agency receiving SBA funds that they would help finance the project and provide technical assistance.

After 1 month of completing forms, 2 months of waiting for processing, and 1 month of setting up how we would work through their procedures, we were finally given working capital in the amount of $40,000 on a weekly basis, as needed.

The technical assistance was in the form of an analysis of computer printouts—for which we had to pay from the amount that was borrowed.

About 6 months into the job in 1978, we were told since the job was so far off schedule we would be given no more money and our loan was being recalled.

We explained that the delay was not caused by us and was on various occasions supported by the owner's engineers.

We were forced to continue the project with no additional money and no technical assistance provided.

After 9 months into the job, the company overall was in desperate trouble and the SBA was calling the loan. We again had to petition for guarantees from our majority partners of the joint venture, and we also needed technical assistance which we could not afford.

An agreement to provide this technical assistance and working capital was negotiated to be paid from the proceeds we would receive from our participation in the joint venture. As previously mentioned, this project began in June 1978 and is scheduled for completion in December 1981 at a profit.

Mr. MITCHELL. Was it completed?

Ms. SMITH. It was completed, 10 percent profit.

Including the processing of these two contracts, the company has now performed over $20 million in transit projects alone. However, even to this day the company faces regulations and intervention by well-meaning persons who feel their interpretation of these regulations concerning processing a contract is with the completion of many forms and constant monitoring, but with no provisions for release of moneys owed or provisions of technical assistance. Our company presently has outstanding claims of over $160,000 from a quasi-governmental agency.

Again, instead of taking away the working capital in actual cash money, this agency has arbitrarily, because of these agreements which have kept a company's 29 employees working, and also allowed the company to look ahead for additional work, decertified our MBE status.

The decertification of our MBE status, which is the company's by virtue of the fact that it is owned and controlled by minorities, has caused the loss of projected income on projects totaling $3.5 million to date.

Further, this decertification is costing the company legal and other fees that could total well over $30,000.

This problem was alleviated as of January 8. We have been recertified.

My testimony is not just to show how difficult it is to start a business as a woman and a minority, but how difficult it is to stay in business and make a business, controlled by a woman who is also a minority, grow.

My testimony leaves out the types of negotiations in which I participated. The constant planning and replanning because doors were closed to me and were opened only when I was accompanied by a man are obstacles that will be alleviated only with the enactment of other formal laws and regulations.

During the months that I prepared the SBA package, on each occasion I had to bring my male partner along to assure that the papers I submitted were accepted, though he made no contribution to the presentation.

It is unfair, but true.

Mr. MITCHELL. Who required that?

Ms. SMITH. The agency.

Mr. MITCHELL. What agency?

Ms. SMITH. MCAP.

At this point I would like to enter as a point of this testimony some suggested approaches to resolving some of the basic business problems that women entrepreneurs face.

The problems faced by women entrepreneurs in business are to a large degree the same as those of any small business; however, they are compounded by a greater amount of past discrimination to overcome, and an inadequate experience history in business due to a lack of past opportunity.

At the core of the problem of past discrimination, the most crucial issue is and always will be under-capitalization.

When you consider the median capitalization amount for women-owned businesses is only $6,700 as reported by the Bureau of Census statistics in 1977, and referencing back to my own beginning with $1,000, you can visualize why this is the major problem of women entrepreneurs.

The analysis of this problem and solution must take into account present day economic conditions and political realities; namely, the announced role of Government appears to be toward less direct assistance and more private sector involvement.

If women-owned and small businesses are a priority to this Government, as it must be, then the role for Government is to treat this priority in the same way it treats, for example, high trade deficits, incentives, capital improvement in updating the country's aging plans and tax incentives.

All businesses have the same capital requirements. These requirements are equity and working capital.

The problem with equity capital is that there appears to be no viable alternative to or reason to substitute individual equity with other forms of investments.

A suggested approach here is to allow for and encourage the infusion of private sector capital in the form of long-term debt and in a more loosely defined sense, nonparticipation preferred classes of stock.

Government should offer incentives for larger firms to invest in women-owned businesses with an eventual eye towards only reaping a return on investment.

In order to accomplish this goal, the larger firm must comfortably feel that investment in small business is good business; by and large that is not a very universally accepted premise at this time. Therefore, it is incumbent upon Government to create these incentives initially.

Even with the free operation of the market, the best managed and operated businesses run into cashflow problems. What is a minor cashflow problem for a majority firm becomes a fight for survival for a woman-owned or minority firm.

Therefore, capital in the form of loans and lines of credit must be made accessible to women and minorities who find themselves shut out because of track record. Government must once again step in to mitigate the perceived risk.

Under working capital the approach for this area of capitalization is enforcement of incentives directly to majority banks to spread the risk of women-owned and minority-owned banks.

Presently such banks are so shackled by regulations that they must, whenever confronted with assisting a minority firm, opt for the most conservative of positions.

To overcome the inadequate experience history in business due to lack of past opportunities, women-owned business technology transfers and training must be accomplished.

As to approaches, Government can devise tax incentives for the encouragement of joint ventures because these ventures may invest assets other than money. There could be some type of offset against ordinary corporate income for this type of transfer; that to assure that there is a division within SBA itself or an agency funded by SBA which can allow for the continual advocacy of women entrepreneur problems and issues.

The problems of women entrepreneurs in the business world are not insurmountable; however, they do indeed require more attention than they are generally given.

In a recent article that I wrote entitled "It's a Woman's World, Too," I used a closing that I think appropriate to close this testimony.

> Women are continuing to make phenomenal contributions to non-traditional fields. From all indications, this trend will continue. The challenge is for women to pursue these fields with haste and diligence. The opportunities are certainly there and await more of us.

But the challenge lies ahead for the Government to lead the way with haste and diligence to make business opportunities for women and minorities a priority—to assure that the success of business and industry in this country can be claimed by men and women.

Mr. **Mitchell**. Thank you very much for your testimony. Let's look at your working capital section. Enforcement of incentives directed to majority banks to spread the risk of women-owned and minority-owned banks.

Presently such banks are so shackled by regulations that they must, whenever confronted with assisting a minority firm, opt for the most conservative position.

Could you enlighten me on that? I know of no banking regulation which specifically impacts on making a loan to a minority firm or a woman firm. I don't quite understand.

Ms. **Smith**. Not being able to speak directly to any specific regulation and being able to only speak from my own point of experience, I would probably say from the area of construction that particular area, speaking very highly of saying that banks only opt to conservative positions, and this was speaking to a vice president of a bank as of last week that contractors have a very difficult time of getting any type of capitalization loan.

Mr. **Mitchell**. Oh, I agree with the problem. I don't agree with what you suggest in the statement is the problem, that they are so shackled by regulations they are forced to take a more conservative position for women and minorities.

I think that is a copout. Frankly I know of no regulations that would impact either directly or indirectly on their ability to make loans to minorities and women. I was trying to—I don't want to press you. Maybe there are some, but I don't know any regulations that would prevent them from making such loans. I think that is a lot of interesting conversation that is offered by bankers as "a justification" for not making the loan.

Ms. **Smith**. Perhaps that is it. It is a justification.

Mr. **Mitchell**. I don't think that is very real.

Your problem was on—let me get at this. Your problem on the attempt to decertify you, am I right in assuming that SBA was attempting to say that you were really not the head of a company?

Ms. **Smith**. Exactly.

Mr. **Mitchell**. That you were a front for a male?

Ms. **Smith**. Exactly. And, as I stated, that has since that time been disproved.

Mr. **Mitchell**. And partially resolved. You are on a temporary recertification.

Ms. **Smith**. The reason I say temporary is because they do not permanently recertify you.

Mr. **Widemire**. This is not SBA.

Mr. **Mitchell**. Who is it?

Ms. **Smith**. MARTA, the Transportation Authority.

It is impossible to get a certification to SBA so you will be permanently certified as a minority or a woman-owned business.

Mr. **Mitchell**. Can you tell me who you are joint venturing this large contract with?

Ms. **Smith**. L. K. Comstock out of Danbury, Conn.

Mr. **Mitchell**. It has been a long time completing it. What caused the delays?

Ms. **Smith**. The delays were engineering problems, scheduling of the project or underscheduling.

Mr. MITCHELL. Were any of the delays caused by some temporary failures of your business?

Ms. SMITH. No; that is why we have the claim. These were all claimable items.

Mr. MITCHELL. One other thing, when did you first start dealing with MARTA?

Ms. SMITH. 1975.

Mr. MITCHELL. At that time you presented yourself as a minority, a woman president of a corporation, right?

Ms. SMITH. That is correct.

Mr. MITCHELL. Did you at that time present them all the data about who controls what percent and so forth?

Ms. SMITH. Yes.

Mr. MITCHELL. That was in 1978?

Ms. SMITH. Yes.

Mr. MITCHELL. Was there ever any question raised about the data that you presented to them?

Ms. SMITH. Not until this year, 1981.

Mr. MITCHELL. Six years?

Ms. SMITH. Six years.

Mr. MITCHELL. Three years later they come back saying we doubt—we don't believe in what you submitted to us initially, is that right?

Ms. SMITH. That is correct.

Mr. MITCHELL. Why do you think that occurred? Was it because you went for a big contract?

Ms. SMITH. Because we at this point—initially on the $9 million contract, we had 5 percent of that contract. We were coming up for another contract on which we were getting 70 percent, which was the majority of that contract instead of the minority portion.

Mr. MITCHELL. That was the point at which there were some questions raised about the legitimacy of your firm?

Ms. SMITH. Right.

Mr. MITCHELL. That is stupid.

Well, there is really not much more I can say to you. I know it is tough, but just as these gentlemen testified, there is a kind of anticlimate that is developing right now across this whole Nation, antiminorities, antipoor. I suppose the only thing that infuriates me is that the personnel in the agencies, instead of combating that climate, it often appears to me that they are aiding and abetting it by finding so many ways to make it more difficult for you to operate and to succeed.

Ms. SMITH. The reason also for bringing up the certification here is that you cannot at this time, as you stated earlier, get permanently certified by SBA.

When I say permanently, I mean if there are various changes in your status as a corporation, you are able to submit that and get your recertification. I would imagine that goes through SBA. We have not gone through that previously.

Mr. MITCHELL. It was my understanding—somebody correct me on this—you were able to get certification, period. Then, as you went through various changes in the growth of your business, you simply reported them in?

Ms. SMITH. That is correct.

Mr. MITCHELL. But there was not such a thing as a temporary certification.

You were either certified or you were not. Is that understanding correct or incorrect?

Mr. WIDEMIRE. Mr. Chairman, this is not an SBA program as far as I know.

Mr. MITCHELL. I am just talking about SBA right now on certification.

Mr. WIDEMIRE. Correct.

Mr. MITCHELL. On SBA, once you are certified, you are certified, it isn't temporary?

Mr. WIDEMIRE. Certainly.

Mr. MITCHELL. Then if there are any significant changes on the part of the company, then that company ought to report to SBA?

Mr. WIDEMIRE. Correct.

Mr. MITCHELL. We are dealing with MARTA in this situation?

Ms. SMITH. The comment I was making is that at present you cannot get in this area or region certified by SBA in terms of certification for 8(a) or whatever programs.

Mr. MITCHELL. You can't?

Ms. SMITH. Our company can't. I can't speak for everybody else. I know we have contacted their office. We have also been sent letters that at present all of the positions or whatever for the program have been filled; therefore, we cannot get certified.

Mr. MITCHELL. This goes back to some earlier testimony where I think it was brought out that SBA would need additional personnel or something to take more people on for certification.

Ms. SMITH. I don't know about that, what the reason is.

Mr. MITCHELL. I just wanted to clear up this business about temporary certification. I never heard of it.

The other thing is does MARTA certify you as a minority firm?

Ms. SMITH. By the fact they accept us as minority firms to participate on their contract after they have gone through our forms and whatever is a fact of certification, but they do not certify us as would SBA certify us.

Mr. MITCHELL. That seems kind of crazy. Well, that is another story.

It seems to me if you have one agency of Government that has certified a firm as being a bona fide 8(a) firm, then why go through all of this other foolishness?

It would be just as if you certified them; then Labor has to come back, the Department of Labor has to come back and do its own certification. That is a waste of time.

Ms. SMITH. The only certification, speaking from my experience, that I know that is universally accepted is SBA certification.

Mr. MITCHELL. I am just curious—and you cannot answer the question—as to why MARTA would not be willing to accept a legitimate certification from an agency of Government.

Questions?

Mr. BLACKISTONE. No, Mr. Chairman.

Ms. SMITH. I don't know whether they do or not.

Mr. MITCHELL. I think it is something we need to look at. I think we need to get hold of the folks there.

In fact, it might be a good conversation for the SBA to have with them, exactly what is the difference between your certification and ours; why can't we use one certifying process?

Thank you very much. Thanks for being so patient and waiting through to the very end.

It is now 1:30. Let's take a short recess until 2:30. Would someone post a notice on the door that the hearings will resume at 2:30?

[Whereupon, at 1:30 p.m., the hearing was recessed, to reconvene at 2:30 p.m., the same day.]

AFTERNOON SESSION

Mr. **Mitchell**. We are now ready to resume.

Several people indicated that they would get here this afternoon to testify. We will accommodate ourselves to that.

I will lead off this afternoon with Mrs. Walker, Enterprise Travel Service, Inc. If you will just come up. She is president of the Interamerican Travel Agents Society.

TESTIMONY OF FLORENCIA WALKER, PRESIDENT, ENTERPRISE TRAVEL SERVICE, INC., AND PRESIDENT, INTERAMERICAN TRAVEL AGENTS SOCIETY, ATLANTA, GA.

Mrs. **Walker**. Good afternoon, Honorable Congressman Parren J. Mitchell, Mr. Clark, distinguished entrepreneurs, ladies and gentlemen.

It is a privilege, certainly a challenging opportunity to give testimony on "How the Government can help small business while simultaneously reducing its own expenditures."

As president of Enterprise Travel Service, Inc. here in Atlanta, Ga., and as president of the Interamerican Travel Agents Society, America's only trade association comprised of minority-owned and operated travel agencies, I am concerned that these minority-owned agencies, individually and collectively, constitute a socially and economically disadvantaged position within the travel industry, which is now the third largest industry in the world.

According to the latest figures published by the Air Traffic Conference of America, there are now 17,339 travel agencies in the United States.

ITAS estimates that approximately only 200 of these are minority-owned and operated. Those 200 thus form only about 1.2 percent of all travel agencies.

When we note that according to U.S. census figures the black population alone—of all the minorities—comprises 14 percent of Americans, we can see that the minority strength in the world's third largest industry, the travel industry, is roughly speaking only one-twelfth of the amount that is proportionate to population.

Thus, it is my view that virtually every ITAS member agency is owned and operated by socially and economically disadvantaged individuals, as those terms are defined and applied by SBA's minority small business and capital ownership development program.

The major role to be played by travel agencies in arranging official Government travel today may be summarized as follows:

One, because of tradition, inertia, and outdated regulations, very few Government agencies have used travel agencies in the past.

Two, nevertheless, all observers are confident that, in the near future, many more Government agencies will use travel agencies, under contract, to arrange official travel.

The roots of today's situation are long and complex. I will summarize them most briefly:

First, from 1945 until just this year, airlines' trade association rules prohibited airlines from paying a commission to travel agencies for sale of official travel by Government employees; thus, travel agencies had no incentive to contract with the Government.

Second, the General Accounting Office and its predecessors had a regulation which prohibits Government employees from using travel agencies to secure domestic travel arrangements; thus, on the other side of the coin, Government agencies were discouraged from contracting with travel agencies.

Finally, until the last year or so, no one within the Government had given much consideration to the advantages to the Government of using travel agencies instead of going directly to the airlines or other suppliers.

Microeconomically speaking, minority-owned agencies are additionally disadvantaged, for in an industry characterized almost exclusively by small business, minority-owned travel agencies are the smallest of the small.

The typical ITAS member, and I believe the typical minority-owned travel agency, grosses about $850,000 a year, which is one-half of the volume of the average U.S. travel agency, according to the Air Traffic Conference of America.

The typical ITAS member then has a gross profit of about $75,000 per year, comprised of commissions, averaged at about 9 percent, from airlines and other travel suppliers such as hotels, rental cars, bus, and railroad companies. The net profit on such amounts is in the range of $25,000 to $35,000 and includes office furniture, cash, and credit. Its liabilities are about $7,500 less than its assets.

Approximately 70 percent of the typical ITAS members' sales are to the minority markets. Minority-owned travel agencies find it very difficult to break into nonminority markets because of traditional buying habits and diminished credit opportunities compared to nonminority travel agencies.

Additionally, ITAS members report difficulty in penetrating even the minority markets because of the failure of the large travel suppliers, namely, airlines, to even attempt to develop such markets, except in the most limited and often superficial ways.

A 1978 GAO report stated:

> Federal employees frequently have not obtained available discount airfares because Federal agencies have inadequate controls and oversight of agency travel. As a result, millions of dollars have been spent unnecessarily on commercial air travel.

In 1980 and 1981 there have been significant, indeed historic, changes in the status quo ante. OMB issued its report on "Strengthening Federal Travel Management" in the summer of 1981. The report recommended that, with total airfare costs estimated at $1.2 billion for fiscal year 1982, the Federal Government should take maximum advantage of commercial travel offices, including travel agencies.

First, the General Accounting Office began to freely grant waivers of its regulation upon request by any Government agency. GAO's willingness to grant ad hoc waivers was first articulated in a report by the Comptroller General entitled "A Look at the Prohibition on Using Commercial Travel Agencies."

That report, prepared at the request of the Small Business Committee's Subcommittee on Special Small Business Problems, stated "GAO would not object to lifting the ban on an individual agency basis to the extent that such action is shown to be more efficient or less costly."

Within the last year four or five Government agencies have requested and received such waivers, and none have been turned down. However, none of the travel agency contractors have been minority-owned or minority-operated.

Second, the Civil Aeronautics Board has overturned the ATC rules prohibiting commissions on travel agency sales of Government travel.

By Order 81-5-20 adopted May 6, 1981, the CAB held that the old anticommission rule was anticompetitive and unnecessarily restricts opportunities of agents to sell and the Government to purchase air transportation.

Thus this expert air transportation agency has found that there is not only nothing inherently wrong with encouraging Government agencies and travel agencies to do business together, but rather I submit to you is, how the Government can help small business while simultaneously reducing its own expenditures.

The Government apparently is finally realizing that travel agents can perform important public benefits, including, but not limited to saving money for the Government.

For example, in July 1980, the Defense Department presented testimony to the CAB on such benefits, and I quote from the direct testimony of Department of Defense, CAB Docket 36595:

> DOD anticipates service improvement and/or dollar economies in the following areas: Reduction in traveler's and supporting staff nonproductive time; reduction of documentation and costs in processing documents; reduction in DOD travel office staffing; production of detailed management reports useful for negotiating volume discounts for transportation, lodging and rental cars; increased use of discounted passenger fares and use of cost favorable routings; increased use of discounted rental cars; increased use of discounted lodgings; waiver of State lodging taxes.

ITAS, of course, concurs with these views, especially those which recognize that travel agencies can reduce transportation costs by finding and using discounted air fares.

ITAS believes that the small number of travel agency procurements will soon proliferate, possibly by geometric proportions.

In the coming year, many Government agencies will recognize the cost savings to be gained by dealing with travel agencies and such agencies, with GAO's approval, will provide many procurement opportunities for travel agencies.

Indeed, in October 1981, GSA issued an RFP covering the establishment and operation of commercial travel agencies for travel services required in connection with Federal Government travelers.

That RFP said nothing about small business set-asides, and it covered travel services to be performed in Washington, D.C., Philadelphia, Dallas, Denver, and Seattle.

In late October and November, there were two new developments.

First, SBA came to GSA and asked that the entire contract be set aside for small business. However, GSA was very reluctant to do so for two reasons.

One, the $2 million size standard restrictions, and

Two, GSA viewed the contract as an experiment and therefore wanted every travel company to bid regardless of size.

Second, GSA added the cities of Baltimore, Des Moines, Raleigh/Durham and Omaha.

After 6 weeks of negotiating back and forth, a compromise was reached. The cities of Washington, D.C., Dallas, Denver, and Raleigh/Durham were not set-aside. The bids were received December 28 from a very large number of companies, according to GSA, including the airlines themselves, American Express, Thomas Cook, Gelco Financial Services and other organizations with thousands of employees.

The cities of Baltimore, Philadelphia, Seattle, Des Moines, and Omaha were the subject of a separate RFP for small businesses, and bids on that RFP are due February 15, 1982.

ITAS members fully intend to try to obtain their fair share of those procurement opportunities. However, two large obstacles loom over the fruition of those intentions:

First, it is likely that the great bulk of Government contracts will be awarded to large travel agencies, such as American Express and Thomas Cook, which have the multicity presence to perform contracts for multisite, multiregional Government agencies; and, second, it is also likely that such set-aside contracts will be awarded to the more established, and better financed travel agencies, even where single office Government agencies are involved.

Both obstacles tend to exclude minority-owned travel agencies from the procurement process.

GSA is still dissatisfied with having to do any set-asides because the $2 million limitation is so low that GSA despairs of getting good low bids out of such small companies.

GSA has, however, been helpful to small businesses by recently holding seminars on how to bid the RFP for travel agencies.

In summary, Government agencies have been dragging their heels in implementing OMB's recommendations; only GSA, as noted, a part of the Labor Department, and a part of Health and Human Services have moved forward.

Why, for example, does the House of Representatives still have a SATO when, as we have been, small businesses can serve equally well or better?

Why doesn't SBA itself make its travel arrangements through travel agencies?

Inertia in my opinion is the only answer. Therefore, ITAS recommends legislation requiring each agency to use travel agencies.

Second, although most travel agencies are small businesses by any reasonable standard, the SBA's current regulations are so outmoded and absurd that most travel agencies capable of performing Government contracts do not fall within the SBA's relevant definition of small: $2 million in gross revenue.

That standard is utterly unrealistic because a travel agency that has less than $2 million in gross sales probably has only three full-time employees.

With such low staff levels, such travel agencies are incapable of performing Government contracts because they do not have the personnel, computerization, and accounting capabilities to be considered responsive bidders under any current Government contract proposals.

As a result, Government contracts cannot and will not be effectively set-aside for small businesses and minority-owned travel agency businesses.

The solution is simple: SBA must amend its size standard to a more realistic level.

We ask that this committee assist us in calling upon the SBA to enact a new, realistic size standard for travel agencies. Thereby it would make our efforts at procurement become successful.

I thank you.

Mr. MITCHELL. Thank you for your testimony.

I do have one or two questions.

You made me feel a little uneasy. When I travel I automatically tell my secretary and we go through the congressional air travel office. I hadn't stopped to think of whether that is a more efficient way to do it through a private, minority entrepreneur.

Mrs. WALKER. I would submit to you you will not only get your ticket, but you will get service; you will get that including delivery.

Among the many other benefits, the thing that is most important is that you will get the best fare and the best routing. When you call an airline, even the SATO, you only get a ticket and you only get what you are asking for at that time. You are not advised of "best fares."

Many of the fares under deregulation, for example, are on an aircraft with the configuration of 90 seats, for example, which may have on that same flight, that same aircraft, four to five, sometimes even six different categories of fares, depending upon many things such as how long in advance you purchase your ticket; another may be whether you are having hotel or car reservations or some other things that will be included along with the ticket that puts it in another fare category.

All of these things a travel agent is aware of and will work for the benefit of not only your convenience, but also the pocketbook.

In a test program with the Department of Labor last year, the contract was awarded to an agency, I think it was called Tauk or Chalk in Washington, D.C.

Without receiving any commissions at all, he proved our point in that test and saved the Government in that 1-year test serving the Department of Labor over $100,000 in airline tickets and in the cost of rental cars and hotels.

The airlines have had a captive market and have lobbied until recently very successfully to maintain the status quo. Now that has been knocked down; the airlines are actually bidding against agents themselves, as I have noted in my testimony.

Mr. MITCHELL. Have you ever tried to do business with a Government agency?

Mrs. WALKER. Yes.

Mr. MITCHELL. What was your experience?

Mrs. WALKER. My experience was that——

Mr. MITCHELL. First of all, which agency was it?

Mrs. WALKER. It was GSA. It was here in Atlanta. They had recently allowed a SATO, which is the scheduled airlines ticket office within a Government facility—which is, if I may say aside, discriminatory, because travel agencies per se are not allowed to put their agencies or businesses in Government buildings.

It is an unfair advantage that the airlines have there.

I was told that after reading much of the testimony before the CAB and others that they did indeed wish to consider the use of retail agents and felt that it would definitely be to their advantage, but they had a period of time to finish the contract that they had already given to SATO, that is, to the airlines to put SATO in their facility.

Mr. MITCHELL. When you went to GSA, you offered your services?

Mrs. WALKER. Yes.

Mr. MITCHELL. You were told that because the congressional offices were in place, that they would not accept your services?

Mrs. WALKER. No. They said that they had an exclusive contract at this point with the scheduled airlines to issue tickets for all Government employees in the Russell Building.

Mr. MITCHELL. You indicated in your testimony that there ought to be some legislation requiring——

Mrs. WALKER. Requiring Government agencies to use travel agencies.

This is supported also by the SBA administrator, Michael Cardenas. I talked with him at the invitation of Fred Williamson of your office, and we met with Mr. Cardenas several months back on this issue.

He agreed that having experienced riding with his son on the same aircraft with his son who was paying $358 to go to California, and although he had gotten his ticket through the accepted means of the Government, his ticket was $660. They were father and son and they were on the same aircraft and they were sitting side by side.

This example is not uncommon.

Mr. O'Malley, who is also with the Small Business Administration, met with me and with Mr. Carl Ellison he indicated that, before coming into SBA, he owned 10 travel agencies and a bus company somewhere outside of Chicago, and that his hope and his total commitment was to try and get the Federal bureaucracy to see and to realize that professionals in the business could certainly handle their travel arrangements better than the secretaries or the various Government employees would.

Mr. MITCHELL. So you have never actually gotten a contract or anything?

Mrs. WALKER. No.

Mr. MITCHELL. Do you know whether any minority travel agencies have?

Mrs. WALKER. No. I know they have not.

Mr. MITCHELL. I don't think I have any other questions. Major?

Mr. CLARK. No questions, thank you.

Mr. MITCHELL. You are right, Mrs. Walker. It is a multibillion industry out there. We are just not in it.

Mrs. WALKER. And we are, as is shown by the way the RFP's are done, systematically excluded.

Mr. MITCHELL. Have you done business with private corporations?

Mrs. WALKER. Yes. We handle travel arrangements for IBM. We do some Avon, and with Metropolitan Atlanta Rapid Transit Authority.

Mr. MITCHELL. Over what period of time?

Mrs. WALKER. We have been doing MARTA since the beginning of the agency. We have been doing IBM tokenism over a year and a half. The same with Avon.

Mr. MITCHELL. I was just wondering. Admitted that the Government has a role to play in assisting businesses in this area, but I am just wondering whether or not the private approach over the long run might not be more lucrative and less burdensome?

Mrs. WALKER. Quite a few of the black travel agencies have been able to contract with large corporations in handling their travel arrangements, but on a basis of affirmative action for those companies who have government contracts and are forced to do it.

It is not done upon the ability and the professionalism of the travel agency that is involved, IBM being a good example of that.

We are a contractor for their services, and we meet a competitive majority company when we make deliveries. We have an envelope with one or two tickets and they have a shoebox full of tickets.

Mr. MITCHELL. Any questions?

Mr. CLARK. Just one question, Mrs. Walker. How would the arrangements be made for you to be paid, assuming that the government agency did in fact invite you to bid for contract?

Mrs. WALKER. In the same manner that they currently pay for their tickets, by GTR, the Government travel request, which the airlines do recognize in the same manner as a major credit card.

So in doing our sales report, if we were to attach the GTR with the auditor's coupon as we would an American Express, then the payment is made directly to the airline that is involved through the ATC central accounting system.

It would not place any undue amount of pressure for cashflow on the travel agency in that sense because the GTR is equivalent to a credit card if accepted by the airline.

Mr. CLARK. In essence then you would be dealing with each Federal employee as they need travel arrangements?

Mrs. WALKER. No. If it is an individual arrangement and it is personal travel, they have the option to use whomever they want. We do handle the travel for many government employees on a personal basis.

Mr. CLARK. No. No. Excuse me.

For example, Congressman Mitchell and I traveled from Baltimore to Atlanta. We may have—Congressman Mitchell may have someone else on the staff traveling from Washington to San Diego or anywhere in the United States. So are you saying that there would be then an exclusive type contract with your agency?

I am a little confused in terms of how you work out the individuality.

Mrs. **Walker**. Not necessarily so, but if you are, for instance, in Baltimore, Jim McLean, who runs a very, very fine travel agency there, if he were called and if your staff there were advised that when making travel arrangements that you call this agency, you would have set up a kind of contract as to delivery, as to time, and to exactly what your needs are in each instance.

They can be specific and different needs for the Congressman than for your travel.

That would be a contract only in terms of how the payment of service is to be performed; but if you are using Government travel requisitions, that would be the payment as far as the payment of an individual ticket is concerned.

If it were on a contractual basis, by government agency then that government agency, under the RFP's that are being offered now, which require that each agency have a capital or cashflow of $1 million.

This, of course, is required in order to bid—because at present they wish to pay agents on a 30-day basis.

They don't want to be in the situation where we have to report on all tickets within 7 days; and if our check was not forthcoming or held up for any reason with paperwork in the Government, that there would be enough cash that the agent would have in order to cover their ticket costs.

Of course, it is not difficult for—as I tried to bring out in my testimony—a Thomas Cook, or American Express, or Gelco Financial System (who incidentally was involved in no way in travel until the RFP's were issued—have no problem with cashflow or having this amount of money on hand.

If we were to be effective in bidding, we certainly would need to be able to have a line of credit which is sometimes not available to minorities, and particularly not available to women as well.

Mr. **Mitchell**. Again thank you. I must stop having these hearings. Every time I have one there is a whole new hearing to be explored and 99 man-hours to be put into this.

It is an area that we have neglected, really. We will take a look.

Mrs. **Walker**. If I may make a closing statement, particularly in regard to Baltimore, Jim McLean is a member of the board of directors of the Interamerican Travel Agents and very, very well informed in the situations that we are all facing, and certainly can articulate the problems that we are facing in the industry and this economy.

Mr. **Mitchell**. He is a good friend of mine. I will be in contact with him. He runs a good business.

Mrs. **Walker**. I am sure.

Mr. **Mitchell**. Thank you very much.

Our next witness is Mr. Greg Baranco from Baranco Pontiac.

TESTIMONY OF GREGORY T. BARANCO, PRESIDENT, BARANCO PONTIAC

Mr. **Baranco**. Thank you, Congressman Mitchell, for allowing me to be here today.

Before we get into the written testimony, I would like to give you a little background on my business. We have been in Atlanta 4 years.

I opened up in April 1978 and I opened a relatively small automobile dealership; I was a franchised Pontiac dealer at the time. We grew—our first year we had total sales of about $6.5 million. We netted about 2 percent. That was great. We had a pretty good year in 1979 and a good year in 1980.

This past year I relocated from East Point, Ga., to Decatur, Ga. I built a new facility financed by Motors Holding Division of General Motors and Bank of the South, a local bank here in Atlanta.

This past year we have done $11.5 million in sales and have had a net loss. The primary difficulty that I have experienced in doing business, beyond the personnel difficulties and so forth that you would normally expect, is that I have a problem in getting operating capital. That problem stems in part from being in business with General Motors, and that means that they discourage our participation with SBA, and last year——

Mr. MITCHELL. They discourage it?

Mr. BARANCO. Yes. The Motors Holding Division of General Motors.

Mr. MITCHELL. Do you know why?

Mr. BARANCO. Motors Holding is an investment company. In good times they have the money to invest with the dealers, so it works very well, but when we reduce inflation by cutting down on the amount of money available in the market, then Motors Holding puts a hold on their moneys and at that point there's no money available for the operator who is an investor with Motors Holding.

Mr. MITCHELL. At that juncture they specifically forbid you to deal with SBA?

Mr. BARANCO. They either want to be in or out. They either want to be the backer or they want SBA to be the backer. So at that juncture, either you have to get together enough money with the bank and SBA to buy out Motors, or you have to stay with Motors.

Right now the problem is that the automobile manufacturers are strapped for cash; so, since they don't have any cash, that means that for dollars on the lower end of the pole, there is little chance of getting additional cash.

Mr. MITCHELL. Could I just ask you one more question?

You had a net loss of $3 million this year?

Mr. BARANCO. No. I had a net loss of a little over $100,000; about $130,000.

Mr. MITCHELL. I am sorry. I had it wrong. You increased your sales by——

Mr. BARANCO. I increased my sales from $6.5 million to $11.5 million. At $6.5 million we had a couple hundred thousand profit. I took all my profit the first 3 years and put it into building a new facility. I have gone out and leveraged everything I have to build this new facility. I have a passive solar facility that is capable of handling a pretty reasonable part of the business in Atlanta, but this past year, in building the facility, in being short on cash, we came from a profit standpoint to a net loss.

Mr. MITCHELL. OK.

Mr. BARANCO. I will continue and go through this.

I am pleased to have this opportunity to present my views and concerns regarding the problems that presently plague the minority business community in this country.

Although my primary purpose is to outline specific responses this committee might make to the minority business community, it should be noted at the outset that it is particularly difficult, if not impossible, for small and/or minority businesses to weather periods of economic recession, soaring high interest rates, and minimal credit availability.

It is therefore necessary that the congressional response to these problems be direct, deliberate, and immediate.

It is with this purpose in mind that I propose the following five-point program to implement these objectives.

Just how effective these responses will be, I don't know, but I do know that there may be one or two suggestions in here that might be worth your attention.

First of all, incentives to the banking community.

Presently the Small Business Administration is charged with the responsibility of making federally backed loans to small and minority businesses.

However, it is suggested that this system is inadequate and that the country as well as the small and minority business community would be better served if banks and lending institutions would become more responsive to small and minority businesses.

To insure such a response from the lending institutions, Congress could provide the following incentives to lending institutions that lend money to minority businesses: One, grant a tax exempt status for profits on loans to minority businesses; two, for moneys earmarked for minority business loans to be available to those institutions at a lower rate of interest.

Mr. MITCHELL. Could we discuss each one of these as we go along?

Mr. BARANCO. That will be fine.

Mr. MITCHELL. I don't know of any other entity in this Nation that gets a 90-percent Government guarantee on lending money as is under the SBA program. Ninety percent.

I have some concern about how much more incentive you are supposed to give. Are you suggesting that maybe we drop the 90-percent guarantee program and instead offer your (a) and (b)? Or is this in connection with the 90-percent guarantee too?

Mr. BARANCO. What I am suggesting is that a businessman is going to naturally have financial ties with the bank. His checking, his normal credit account, accounts receivable, so forth and so on. What we want to do is get into the normal mainstream of doing business. There is not an SBA available in every community.

For example, in metro Atlanta. I am in Decatur and if I need to deal with the SBA, I come to Atlanta. That is not a big deal, but there are banks I pass on every corner. These are lending institutions that are charged with the responsibility of participating in these communities to help them grow.

These bankers are not going to lend money to the minority businessman because of the high risk.

He is automatically the new businessman.

Mr. MITCHELL. That is why he has a 90-percent guarantee.

Mr. BARANCO. I don't question that, but are these the results we are after?

Mr. MITCHELL. No, they are not.

Mr. BARANCO. What I am saying is we have a banking community that is established. What we need to do is go to those bankers and find out what incentives they want that will help them to respond to the minority and small business community. I don't know that these are the answers, but I did get these from talking with the bankers that I happen to know.

Mr. MITCHELL. Then I am going to work on the assumption that your (a) and (b) would be for those banks that are not participating presently in the bank guarantee program. It wouldn't be a triple dip?

Mr. BARANCO. That is correct.

Continuing, enforcement of present laws.

There are laws presently in existence which, if enforced, would alleviate much of the disproportionate treatment received by minority businesses. The Equal Credit Opportunity Act is an example of a law that needs to be strictly enforced.

We were talking earlier, Mrs. Walker was talking about set-aside programs. You know, if these programs were followed through with the minority businesses that are here and their adherence so that these programs had a success rate—and I don't mean just numbers—I mean that you have numbers of businesses participating, I think that would help a lot of the problem.

So the small SBA program with the 90-percent guarantees, you know if the majority of the businesses that are out there now had participated in those types of programs, I think they would be better off as a result.

Mr. MITCHELL. Oh, I think so, too. My only concern is that even with that kind of cushion, a fantastic 90-percent guarantee, we still didn't get maximum bank cooperation.

That is why we had to establish the direct loan program. Again I just question how much do you really have to give to get the kind of cooperation that we would want to make these programs successful?

Mr. BARANCO. Maybe some of it. I don't know, but if the banks have not begun to participate, we have not found the answer.

Mr. MITCHELL. No.

Mr. BARANCO. Somehow we have got to get with the bankers and get them to help us decide what it is going to take to have their participation.

No. 3, representation in decisionmaking positions.

Congress should urge banks and other lending institutions to cause their respective boards of directors, branch managers, and other decisionmaking positions to be reflective of the communities they service.

I don't think you can make a bank put anybody on their board of directors or promote people up through the bank. When I go to talk with somebody about some money, it is very seldom that I am talking to a black or minority banker with the authority to make a loan—other than to buy a car—but I am talking about business loans.

I think that if there was some responsiveness in that area—I don't know how you would get about it—but if there were people who were familiar enough with minority persons that they could make a decision as to the credibility of the individual, that would help.

Mr. **Mitchell**. All right.

Mr. **Baranco**. No. 4, the continuation of minority enterprise small business investment companies [MESBIC's].

It is my belief that MESBIC's can be an important element in the economic future of minority businesses. It is my hope that Congress will continue to support the present MESBIC's and encourage the formation of new MESBIC's.

However, it is suggested that these organizations would be more effective and more responsive to minority businesses if their respective boards of directors and decisionmaking positions consisted of business persons.

I made that statement because at one time there were several MESBIC's and several of them are not in existence any more because they were more tilted toward social loans than business loans.

There are qualified minority businesses out there that need some avenues for money, and in quite a few places the MESBIC's are not in existence any more.

I think their lack of existence was because of the makeup of the people running the MESBIC's.

No. 5—and I think this is one that if there is some way we could implement this, it would help quite a few of the businesses.

Require foreign businesses to participate in a set-aside program with minority companies.

Foreign companies doing business in the United States should be required, as an incident of doing business in the United States, to transact 10 percent of their business through minority firms, distributors, dealers, et cetera.

Mr. **Mitchell**. Intriguing idea. I think the Baltimore Hilton in my city is Kuwaiti-owned. Obviously there is an ever-increasing amount of foreign investment in the United States. It is an intriguing idea.

I can see the State Department getting into the act and half a dozen other people, the CIA and somebody else, but at least it is something worth exploring.

Mr. **Baranco**. Well, there are quite a few dollars, businesses being transacted by foreign businesses in the United States. These businesses—for example, a Toyota——

Mr. **Mitchell**. There is really no flow of money into our community, at least theoretically, in the profits that are made.

Mr. **Baranco**. That is correct.

Mr. **Mitchell**. If a Kuwait company owns the Hilton in Baltimore, they take that money out, those profits, and that goes back to Kuwait, I would guess. I would think it might well be a good idea to pursue the possibility of how we can get a better flow of some of those profits into our communities.

Mr. **Baranco**. Take the General Motors, Ford, Chrysler; there is a social pressure to have minority participation to reflect the community they exist in; but for these foreign firms, particularly in the car business, there is none at all; yet they have a third of the business.

Mr. MITCHELL. It certainly is an interesting recommendation I would like to take a look at.

Although, as I said, I can see Commerce talking about foreign trade zones; the State Department getting into it; AID, everybody else.

I am being facetious now. It is one we ought to try to pursue.

Mr. BARANCO. I trust these suggestions are responsive to your inquiry. However, if you have further questions, please direct them to the undersigned at my post office box.

Mr. MITCHELL. Unfortunately, send them through the post office.

I did very badly in chairing this segment because I kept interrupting you.

Mr. BARANCO. That is all right.

Mr. MITCHELL. I have used up all of my questions.

You did have some ideas that caused me to raise questions immediately. Thank you.

Mr. CLARK. No questions, Mr. Chairman.

Mr. BLACKISTONE. No questions. Thank you, Mr. Chairman.

Mr. MITCHELL. Thank you very much.

I believe there are two other witnesses to be heard from. Mr. Gordon Bradl?

Mr. Bradl, thank you for being here. You are going to lose a lot of money today by taking off from business. We cannot reimburse you for your business losses that you will incur because you are kind enough to come before us.

I do thank you.

TESTIMONY OF GORDON BRADL, VICE PRESIDENT, BANK OF THE SOUTH

Mr. BRADL. I am glad to be here. Do you have a copy of my rather limited testimony?

Mr. MITCHELL. Yes, we do.

Mr. BRADL. If you would like me to read it, I would be glad to. Otherwise, I would be happy to answer questions.

Mr. MITCHELL. Why don't you speak briefly to highlights in your testimony? Then we will raise some questions.

Mr. BRADL. First of all, I have been in lending for quite a number of years. I have utilized Government programs. I have found them to be effective, particularly the SBA, over a long period of time, both out of State and within the State.

It has always been my feeling that the type of businesses that you would put an SBA guarantee on carry above ordinary risk and above ordinary terms and, therefore, they require above ordinary rates if you are considering them as part of your normal portfolio, regardless of whether it involves minority or any other type of business.

I think I stressed I feel that the program itself has been one of the most beneficial of Government programs that I have ever seen in terms of the fact that if you do have one successful loan or operation through the furnishing of a guarantee, Government guarantee, then you have expanded your ability to generate jobs, purchase goods and services; it has a multiple effect that we often talk about, but rarely see in action.

The one example that I give here in my testimony is the Metalux Co. in Americus, Ga.

It is just such a fantastic example. There have been others, very similar, throughout the country.

I think the main thrust that I would also give, one of the prime areas that you were to address here as I understood it, was the rate consideration. In conversation about reducing the rate to prime or some other level because of the guarantee furnished by the Government agency.

For the reasons I enumerate there, I think that would effectively shut off this program and make it that much more difficult for other people trying to start a new business or expand a business or receive temporary help.

It would close them out of the market because of the requirements for prime rate on extended terms and above average risk type loans. That just doesn't excite people that lend money.

Mr. MITCHELL. Apparently you are one of the enlightened lending institutions. That makes me doubly glad to welcome you here.

[Mr. Bradl's prepared statement follows:]

PREPARED STATEMENT OF GORDON BRADL, VICE PRESIDENT, BANK OF THE SOUTH

I am currently a Vice President at Bank of the South, N.A., Atlanta, Ga., involved in commercial lending. Although the bank has worked with and had a strong interest in "small business", the views expressed herein are solely my personal observations. These are based on over 20 years lending experience involving small and medium size business, as well as large companies, and using various government guaranteed lending programs, among them, the Small Business Administration.

Most small businesses operate with limited capital and therefore, are highly dependent on borrowed money to continue operation regardless of economic conditions. This leverage magnifies the owners' rate of return when successful and works in reverse when unsuccessful. Thus, failure rates are high, particularly in new ventures. In my opinion, the SBA basic business guarantee programs have addressed this problem. There have been many successes. One notable example in our State is the Metalux Company, Americus, Georgia (Multimillions in sales and several hundred employed). These successes have a multiplier effect far beyond their own communities; contributing to the national economic well being through higher employment, increased purchases of goods, and services while enhancing the entreprenurial spirit that made this country a world leader. Consequently, I strongly endorse the Small Business Administration basic guarantee programs. This does not mean that guarantees should be granted to lenders under those programs willy-nilly. Because of the above average risk in such lending, the lender should feel strongly about the prospects for success, feel confident about the owners' basic capabilities and then, because of lack of sufficient capital and/or established cash flow to service the proposed loan, seek a guarantee to minimize that risk.

One of the propositions being discussed—reducing the rate on guaranteed loans to prime (however that is defined)—would result, in my opinion, in a sharp curtailment of such loans. The practical effect would be to close out the possible successes which can absorb the losses that you would expect and will occur under this type program. Because of the above average risk and terms, these type loans should carry an above average interest rate. Despite the SBA guarantee, most loans are of a long term nature, five to fifteen years, and require above average attention.

You should also note my stress on SBA basic business guarantee programs. The availability of SBA guarantees for farmers, an area in which the agency had no expertise, has led to significant loan problems and will cost millions of taxpayer monies. This has created an unnecessary black-eye for the mainstream SBA guaranteed lending programs. Any program such as this is subject to abuses. But my best testimony as to viability and desirability of the SBA guaranteed lending programs is the successful graduates.

Mr. MITCHELL. You do participate in the bank guaranteed loan program?

Mr. BRADL. That is correct. Other than just SBA. I want to stress in my testimony that anything I say here is my own personal view as opposed to my institution's view.

Mr. MITCHELL. From your own personal point of view, would you react to some plans that were proposed this year that have been scuttled but I am certain that they will resurface again?

One such plan was to reduce the amount of the guarantee. In discussions with both the Senate and SBA, at one time it was talked about reducing the guarantee to 50 percent or 60 or 70 percent, anything but 90. I think we won that battle for last year, but I am certain it will be enjoined again.

What is your reaction to something less than a 90-percent guarantee?

Mr. BRADL. When the SBA was in the direct lending business, they used to provide a 75-percent guarantee. We discussed this at length in our Small Business Advisory Council meetings over a period of time. I think the net effect of that would be to upgrade the credit standards that a lender would be looking for in a particular loan that would have a Government guarantee attached to it.

I think that would be more beneficial than a rate reduction approach. The thing is, it will shut out people, but historically it is when things are difficult that people are very inventive and find ways to do things.

They borrow capital from relatives. They turn up sources that you don't dream about and many times a deal can be put together. Most deals are changed many, many times before you get to the final product. People have been turned down many times.

I can think of one case in my own situation; I turned a fellow down four or five times. He finally came back and got it to the point where the deal was put together. So it is a question of persistence. Not everybody should be in business for that matter. The failures are the ones that usually get all the attention and publicity of the abuses in the program. That is why I feel strongly about the SBA program. Whether it is in the 75 or 90 percent category, there could probably be a split where certain cases are 75 percent; others are 90.

Mr. MITCHELL. That was the compromise that took place. I wasn't very happy with it, but it has been effective—you personally, not for the bank. I have a feeling that much of the loss rate that SBA sustains on its loans—particularly their direct loans—is attributable in part to the ratio between the loan officers and the volume of loans.

At one point I think I heard where one loan officer in the SBA might handle as many as 500—was that right—500 loans in his portfolio? How do you handle that in your bank? Is there generally an accepted ratio of number of loans to personnel?

Mr. BRADL. It depends upon the complexity of the credit involved. In other words, it is conceivable that one person could spend all of their time on one particular company if there are problems involved.

When you are talking about usually a marginal-type loan such as you——

Mr. **MITCHELL**. These are automatically marginal because they are direct.

Mr. **BRADL**. That is correct. They require above average attention to start with. Anybody that feels that he can handle even 100 marginal loans is fooling himself regardless of how good he is unless he has a superstaff to fall back on.

I would say there are no accepted norms that I know of. Banks historically have tried to run out statistics on that. One person can service a portfolio of $60 million to $70 million, several hundred loans, but they may be loans that don't require a lot of attention. You can lend to good credits much easier.

Mr. **MITCHELL**. If you were the chief officer there at SBA and you knew that you were dealing with risk loans, would you try to establish a ratio?

Mr. **BRADL**. I don't believe I would try to establish a ratio. I would try to establish a much better follow-up program. That is where SBA has historically fallen down very badly. Their inability to move rapidly with a deteriorating loan situation.

You have to be able to take action quickly; otherwise the value of your security disappears. I think there has been a reluctance many times by the SBA to pursue that.

Mr. **MITCHELL**. If the guy is handling 500, how can he move rapidly?

Mr. **BRADL**. Obviously the case you are citing would be he has no opportunity to do anything really. He is just running around putting out fires.

Mr. **MITCHELL**. Sure he is.

Basically you support the SBA efforts. Basically you have indicated that there are successes that you have been instrumental in providing. You cite one here. On the right, you are suggesting that there not be any reduction of the rate or recommending that there not?

Mr. **BRADL**. That is correct. I think in the secondary market there is a reflection of the guarantee by the Government agency, the secondary market that helps provide additional funds; but that goes beyond the borrower, of course.

Mr. **MITCHELL**. Could I ask you, have you made loans to farmers?

Mr. **BRADL**. Not myself personally, but I was against the entrance of the SBA getting into that program and so wrote the director at that point in time.

Unfortunately, the Senator from our State was instrumental in getting SBA in that particular program.

Mr. **MITCHELL**. Then you are not in a position, really, to comment on a question I raised earlier about abuses in that program?

Mr. **BRADL**. No. Other than what I have read in the newspaper.

Mr. **MITCHELL**. Don't ever believe that.

Mr. **BRADL**. The only other comment I would have would be the fact that the volume of loans in that category that are delinquent, it would be—getting back to the situation you mentioned about the number of personnel to service them—it is just not feasible. It will result and has resulted in considerable chargeoffs that affect all of us in our pocketbook.

Mr. **MITCHELL**. I certainly know that anyone with any intelligence would not countenance abuse in the programs. I look at Buffalo, N.Y., for example, this winter where they got some 50 inches of snow and then 2 weeks later another 59 inches of snow.

A lot of those businesses are going to ask for disaster loans, for example. These are not farmers. Maybe farmers in the area, too.

If this spring, instead of snow they get flooding, this guy is almost bound to default or bound to become delinquent at least and for a long period of time.

Questions?

Mr. BLACKISTONE. I have two questions.

First, what has been your bank's experience this year in making guaranteed loans with the high interest rates? Have you found there has been less demand for guaranteed loans?

Mr. BRADL. I would say yes.

Mr. BLACKISTONE. Significantly less?

Mr. BRADL. I can't speak for that because we don't keep a central reporting site for SBA loans.

Our branch managers handle all retail type activities, as an example. The request would come through me because of my tie with the SBA.

We would automatically funnel it out to the branch that would be appropriate.

Mr. BLACKISTONE. The second question is, do you normally retain the guarantee loans you make or do you sell them on the secondary market?

Mr. BRADL. We retain them because we have never made that determination to be in the program on a full continuing basis.

In other words, it would fluctuate in accordance with economic conditions.

Mr. BLACKISTONE. I am not sure I understand.

Mr. MITCHELL. Would you pull the mike a little closer to you?

Mr. BRADL. What I am suggesting is that to be in the secondary market means that you make a commitment to develop a servicing portfolio of these type loans and that you automatically sell them in good times and bad. We have never made that policy decision to go into it on that basis.

So, therefore, we have retained all the loans that we have ever made that bear a guarantee.

Mr. BLACKISTONE. So it could conceivably happen that the bank could decide to get out of the guarantee program one day?

Mr. BRADL. As with any type of lending program, we are subject to cutting it down or cutting it off if we so felt. That is correct.

Mr. BLACKISTONE. Is that generally the policy of banks in this area, to not sell on the secondary market or do you know?

Mr. BRADL. I can't say because I don't know how they handle their portfolios.

Mr. MITCHELL. Major?

Mr. CLARK. Does your bank participate in the bank certification program?

Mr. BRADL. We are qualified to do that. I am not aware of any BCP loans that have been done.

Mr. CLARK. Are you aware of any comparison or type of analysis between the rate of approval for the bank certification program versus the regular guarantee program?

Mr. **Bradl.** Just my own personal experience. I have always had the good fortune to have loans approved in a very short time regardless of going under the regular program. Therefore, we have not had the need to get into the BCP program.

Mr. **Clark.** Thank you.

Mr. **Mitchell.** Thank you again very much.

Mr. **Bradl.** Thank you for letting me appear.

Mr. **Mitchell.** Let me just chat with you for 1 minute. It is an interesting commentary on America that here in this hearing we are really dealing with the nuts and bolts of the American economy.

How do you protect small businesses, foster the development of minority businesses? If this were on foreign affairs of some sort—what are we going to do with Poland, how do we control Menachem Begin—there would be a room full of people.

But it is an interesting commentary that on something as important as this—to see whether the laws on the books are working or how we can make them work for, really, the backbone of this Nation—there is relatively little interest.

I just wanted to share that with you so maybe you can become one of the—you already are, but an enhanced advocate of minority business and small business, to suggest the importance of this kind of information gathering.

Mr. **Bradl.** I would like to make one comment to you, Mr. Chairman. I believe it was in 1965 or early 1966 that the minority program began. At that time they offered 100-percent guarantees. We made the first guaranteed loan under that proposal when I was with another lending institution in the State of Georgia.

It has been my experience that the failure rate was very high at that level.

Mr. **Mitchell.** Thank you. Thank you very much.

I thank all of the witnesses.

Do we have any other witnesses? I think we have covered every witness who asked to be heard.

I thank all of you who stayed with us all day. With that we will conclude the hearing for today. Thank you very much.

[Whereupon, at 3:40 p.m., the committee adjourned, to reconvene subject to call of the Chair.]

APPENDIX

Appendix A.—Additional Questions Submitted to and Responses Received From the Arizona Banking Community

MAJORITY MEMBERS
PARREN J. MITCHELL, MD.
CHAIRMAN
NEAL SMITH, IOWA
JOSEPH P. ADDABBO, N.Y.
HENRY B. GONZALEZ, TEX.
JOHN J. LAFALCE, N.Y.
BERKLEY BEDELL, IOWA
FREDERICK W. RICHMOND, N.Y.
HENRY J. NOWAK, N.Y.
THOMAS A. LUKEN, OHIO
ANDY IRELAND, FLA.
IKE SKELTON, MO.
BILLY LEE EVANS, GA.
CHARLES W. STENHOLM, TEX.
ROMANO L. MAZZOLI, KY.
NICHOLAS MAVROULES, MASS.
GEORGE W. CROCKETT, JR., MICH.
CHARLES HATCHER, GA.
RON WYDEN, OREG.
DENNIS E. ECKART, OHIO
BYRON L. DORGAN, N. DAK.
GUS SAVAGE, ILL.
BUDDY ROEMER, LA.
JOHN G. FARY, ILL.

Congress of the United States
House of Representatives
COMMITTEE ON SMALL BUSINESS
2361 Rayburn House Office Building
Washington, D.C. 20515

MINORITY MEMBERS
JOSEPH M. MCDADE, PA.
SILVIO O. CONTE, MASS.
J. WILLIAM STANTON, OHIO
WILLIAM S. BROOMFIELD, MICH.
DAN MARRIOTT, UTAH
LYLE WILLIAMS, OHIO
OLYMPIA J. SNOWE, MAINE
DANIEL B. CRANE, ILL.
JOHN HILER, IND.
DAVID MICHAEL STATON, W. VA.
VIN WEBER, MINN.
HAL DAUB, NEBR.
CHRISTOPHER H. SMITH, N.J.
ED WEBER, OHIO
DAVID DREIER, CALIF.
GUY V. MOLINARI, N.Y.
MARK D. SILJANDER, MICH.

[illegible], STAFF DIRECTOR
[illegible], GENERAL COUNSEL
[illegible], MINORITY COUNSEL

MAJORITY—[illegible]
MINORITY—[illegible]

AREA CODE: 202

Mr. Nate Collins
Vice President of Corporate Banking
Valley National Bank
P.O. Box 71
Phoenix, Arizona 85001

Dear Mr. Collins:

I would first like to thank you for being a witness at our September 1, 1981 field hearing in Phoenix, Arizona.

Second, because of time constraints, I was unable to ask a number of questions of you and the other representatives of the Arizona banking community. To complete our hearing record, would you kindly submit to me in writing answers to the enclosed questions, which are being submitted to all bank representatives.

Your assistance to the Committee is deeply appreciated.

Best wishes

Parren J. Mitchell

PJM:nka

Enclosure

Since the SBA sets the maximum interest rate on guaranteed loans based on a "prime plus" formula,, the agency is now questioning the need for the "plus" if in fact prime no longer represents the best business rate available.

1) What interest rates are you charging on SBA guaranteed loans?

Is the rate a floating rate tied to prime or is it fixed?

2) What loans have you sold in the secondary market?

What spread or rate do you retain as a service fee?

3) Does your bank make commercial loans at interest rates below prime or base rate?

Under what circumstances?

e.g. short term of days or months?

with compensating balances?

with points?

4) Could you supply the Committee with a random sample of commercial loans now in your portfolio showing:

a. date the loan was made and prime rate that date

b. rate of interest, and designating either fixed or floating

c. amount of loan

d. term of loan

e. effective yield (after considering other income)

Valley National Bank of Arizona
HEADQUARTERS: PHOENIX, ARIZONA

NATHAN C. COLLINS
SR. VICE PRESIDENT

P. O. BOX 71
PHOENIX, ARIZONA 85001

ktd 9/81
[illegible]

October 13, 1981

RECEIVED
OCT 19 1981
PARREN J. MITCHELL

Congressman Parren J. Mitchell, MD
Committee on Small Business
2361 Rayburn House Office Building
Washington, D.C. 20515

Dear Congressman Mitchell:

It was an enlightening and pleasant experience to have served as a witness for you at the September 1, 1981, fall hearing on small business. Listed below are our Bank's responses to your questionaire included in the letter we received from you on October 5, 1981.

1. The interest rates we currently charge on SBA guaranteed loans all float with prime and typically are at or near the allowed maximum.

2. We have sold no loans into the secondary market. However our taking that under consideration is a possibility for the future.

3. We do not solicit commercial loans that are priced below prime, but will on selected occasions do so under the competitive pressures usually created by out-of-state money center banks. The funding of these loans would ordinarily be done on a particular basis for a period of less than 30 days and on a funds available environment. Typically these would have no other compensation requirements.

4. Well over 65% of all loans in our commercial portfolio are now made to float with prime rate with a target yield that will provide a 2% spread. Due to the administrative costs, smaller loans tend to bear a higher rate on the range of 1/2%. Typically any loans beyond one year will carry an additional premium of 1/4 to 3/4 of a percent.

Congressman Parren J. Mitchell, MD 10/13/81
Committee on Small Business Page 2

Our Bank and the marketplace finds us in a capital deficient environment. Therefore, we do not find ourselves compelled to engage in price cutting on interest rates. We believe the two elements most important to small business is the availability of funds and a cost that will be reduced through the general reduction in interest rates across the country. Such action would preclude the need for reducing rate spreads charged by the lenders.

I hope this will be of some help as you champion the cause for small business. Again, I feel honored to have had the opportunity to appear before your committee and will watch with interest as this legislative year gets underway.

Sincerely,

Nathan C. Collins
Sr. Vice President and Manager

NCC/bmk

Dictated but not read by Nathan C. Collins.

THUNDERBIRD BANK

John E.Hansgen
Senior Vice President
Business Loan Division

Member F.D.I.C.

October 15, 1981

Mr. Parren J. Mitchell, MD.
Chairman
Congress of the United States
House of Representatives
Committee on Small Business
2361 Rayburn House Office Building
Washington, D.C. 20515

Dear Mr. Mitchell:

I was pleased to appear as a witness at your field hearing held in Phoenix, September 1, 1981.

Hopefully, the attached is satisfactory in answering the questions needed to complete your hearings. Please bear in mind that we are one of the smaller banks in the area and are heavily oriented to the small and medium size market segment.

Because of our size, we tend to be more "asset managed" as compared to "liability managed.' Approximately 25 percent of our loan portfolio falls under the SBA quaranty program and the "Peg Rate" is utilized as a base on all SBA loans.

Obviously, we could not price all loans in the portfolio on this basis. However, we do find that our method has worked well for both the customer and ourselves. Utilization of the variable peg has cushioned our customers from the volitility associated with prime and has helped us stay reasonably in line with the rising cost of funds. We also feel the cushioning effect has contributed significantly to our success in the program due to fewer workouts and failure problems.

Permit me to express our appreciation to you for holding hearings in Phoenix. Both my colleagues and I commend you on your awareness and knowledge of, both the problems facing small business, and the SBA program. Keep up the good work.

Please do not hesitate to call on us whenever we can be of assistance.

Respectfully,

John E Hansgen
John E. Hansgen

JEH:bs
enc.

2031 W. Camelback Rd.
P.O. Box 11856
Phoenix, AZ 85061
602/242-1111

ANSWERS TO QUESTIONS

1. All loans are priced on a variable rate. The initial rate is based on the spread over prime and is adjusted to the spread over SBA peg rate after two calendar quarters. The rate is adjusted in accordance with the SBA peg semi-annually. The guaranty fee is passed on to the borrower.

2. We have not sold any loans in the secondary market since 1974. At the time, servicing fees ranged from 1/4 of 1% to 3/4 of 1%.

3.&
4. The following policy guidelines in force cover both 3 and 4 of the questionaire:

   a) All commercial loans, other than SBA guaranty loans, are priced with a spread utilizing prime as the base.

   b) As a general rule, the interest rate is variable with a floor. Occasionally, a fixed rate based on price is used on loans of short maturity.

   c) Compensating balances are taken into consideration in determining the spread over prime on an informal basis. The spread normally varies between 1% and 3%.

Copper State Bank

P.O. BOX J, APACHE JUNCTION, AZ 85220 • TELEPHONE 982-0600

October 19, 1981

Mr. Parren J. Mitchell
Chairman-Committee on Small Business
2361 Rayburn House Office Building
House of Representatives
Washington D.C. 20515

Honorable Mr. Mitchell:

As you requested in your recent letter, answers to the questions you submitted as follow up to my testimony before your committee on S.B.A. Program are as follows:

1] Copper State Bank's interest rates on S.B.A. loans are presently tied to floating rate of prime plus 1 or 2 percent.

2] Copper State has sold approximately $500,000 worth of loans on the secondary market in 1979. We have retained ¼ of 1% as a service fee.

3] We have made a number of loans at below prime. Most of these loans are for one year or less. Some would be secured by passbooks or TCDs; others would be with 3 or 4 points.

4] Within the year 1981 our loans were made at prime plus 1 or 2 percent. Most of these are floating on an adjusted quarterly basis. We have recently converted our loan portfolio from hand posting to computerization and, as of September 1, 1981, all loans have been going on our books at prime plus 1 or 2 percent, adjusted daily. Our loan limitation is $200,000 and, therefore, our commercial loans

Copper State Bank
P.O. BOX J, APACHE JUNCTION, AZ 85220 • TELEPHONE: 982-0600

October 19, 1981
Honorable Parren J. Mitchell
Committee on Small Business
House of Representatives
Washington, D. C. 20515

4] CONTINUED

range from $5,000 to $200,000. The terms range from 30 days to one year and the effective yield is the APR disclosed on these notes. The exception to this is construction loans where we charge up to 4 points and the yield could range as high as 28% and this is disclosed as the APR on the disclosure forms.

It was a pleasure to be of assistance to your Committee. Contact me if I can help you in any other way.

Sincerely yours,

Robert E. DeBow

ROBERT E. DeBOW
President/Board Chairman

RED/jm

THE Arizona BANK

E. DANSON PERIN
EXECUTIVE VICE PRESIDENT

November 24, 1981

The Honorable Parren J. Mitchell
Congress of the United States
House of Representatives
2361 Rayburn House Office Building
Washington, D. C. 20515

Dear Congressman Mitchell:

I much appreciated the chance to testify before you during your recent visit to Phoenix, Arizona. I would like to respond to some of the questions outlined in your letter addressed to Mr. Robert Matthews several weeks ago.

The prime rate of The Arizona Bank is defined as that rate of interest which the bank establishes from time to time by directive to its lending and branch divisions as a basis for determining the interest rate to be charged on certain commercial and personal loans. The rates that we charge on SBA guaranteed loans generally float and are tied to The Arizona Bank's prime rate. The rates that we charge range from one percent above prime up to the maximum allowable rate on SBA guaranteed loans. Thus far we have not sold any loans in the secondary market, but that is an option which we might choose to exercise at some point in the future.

Your third question concerned sub-prime lending. This kind of lending activity on the part of banks is rather sporadic and tends to occur as short-term rates begin moving lower. The prime rate is stickier than money market rates, and as overnight rates come down producing a widening gap between the prime and money market rates, below prime lending activity picks up. As rates flatten or move up, this kind of lending tends to diminish and disappear altogether.

Our bank has made commercial loans at interest rates below prime rate. In our national division, we have participated in several syndicated loan agreements to multi-national companies that give the borrower the option to borrow at rates based on the prime rate or the Eurodollar rate. Because Eurodollar rates sometimes fall below domestic rates, actual borrowings have carried a rate below our stated prime rate. There are only two or three such loans in our bank. In each case, the borrower pays fees and also carries balances with us. From a practical standpoint, most of these companies borrow in the commercial paper market anyway, and as a consequence, these backup facilities are rarely used. In a few selected instances, we have loaned money from time to time to companies below the prime rate on an overnight basis. In the several instances to which I refer, the borrowers are very substantial customers of the bank possessing the highest credit quality and have extensive credit and non-credit facilities with us. This kind of activity is extremely limited at The Arizona Bank, and in each case, the overall yield to the bank exceeds the prime rate because of balances, fees, other credit and non-credit activities and the low overall cost of servicing such borrowings.

Rather than give you a random sample of commercial loans, it might be more helpful to give you some ballpark facts on our commercial and industrial loan portfolio. Our total commercial loan portfolio totals approximately $475,000,000. The two largest areas are the national division, which in our bank handles national and multi-national corporations and the commercial loan department, which has responsibility for local, small- and medium-sized companies. These figures will all vary from time to time, but the average prime rate for the month of September, 1981 was 20.08%. The average yield for the national division was 21.23% and for the commercial loan department, 20.9%. These yields include fees but do not include any credit for balances, so the overall yield would be significantly higher than the figures I gave you.

I hope this information will be of use to you. If I can be of any further help, please let me know.

With best regards,

E. Danson Perin
Executive Vice President

EDP/ay

APPENDIX B.—STATEMENTS RECEIVED FOR INSERTION IN THE SEPTEMBER 1, 1981 HEARING RECORD

August 25, 1981

TO: Committee on Small Business
House of Representatives
Congress of the United States

FROM: Litton Industries
Electro-Optics Department
Tempe, Arizona 85281

IMPROVING THE EFFECTIVENESS OF PROGRAMS OF THE FEDERAL GOVERNMENT FOR SMALL BUSINESS AND SMALL ECONOMICALLY DISADVANTAGED BUSINESS

This statement is submitted in response to a request for testimony at the field hearing by the House Small Business Committee to be held in Phoenix, Arizona on September 1, 1981.

Litton Industries wishes to preface its statement by putting the Electro-Optics Department into proper perspective relative to other Phoenix area businesses serving as prime contractors to the U. S. Government. While we are a facility of a major corporation, we are quite small in comparison to many of the Phoenix area companies. We employ only about three hundred (300) people and would ourselves qualify for small business status did we not have our corporate affiliation. We have been in business in the Phoenix area for five (5) years. Our major customer is the Department of Defense. As a prime contractor of the U.S. Government we are ethically and contractually obliged to conduct our business in accordance with DAR 7-104.14. Public Law 95-507 provides the guidance and direction for this DAR. We are and have been in full and complete compliance with the requirements set out by the law and the Defense Acquisition Regulation. During the period of October 1980 to June 1981 our Department has committed about 74% of all its purchases to Small Business and within that percentage about 3.2% to Small Economically Disadvantaged Businesses.

In the performance of our business and in our continuing efforts to involve Small Business and Small Economically Disadvantaged Business with sub-contracted requirements we encounter some difficulties. It is from this limited experience that we draw in order to pose some ideas for possible consideration by this committee.

We are engaged in a very specialized high technology manufacturing area and our products (viz. Night Vision Devices) are exclusively configured for the demanding requirements of the U. S. Military. Most of the items we purchase for our products are made to military specifications and/or drawings, very few are catalog type items. In a significant number of instances we find that new or recently started Small Businesses and Small Economically Disadvantaged Businesses are little prepared to cope with the requirements which the U. S. Government requires us to pass on to our suppliers and subcontractors. Particularly in the area of technical data reports, certifications, and quality control do we find this to be so. The level of technical skills and awareness needed on the part of the subcontractor is also sometimes lacking. We believe that this is not a situation unique to Litton. We think that prime contractors such as ourselves can help greatly in these instances. For instance, we have found it highly beneficial to dispatch engineering, quality control, and purchasing specialists to small businesses prior to any contractual involvement. These specialists help the potential subcontractor in fully understanding the technical and quality requirements and the necessary capabilities and resources to meet those. After an order is placed the same specialists can be made available to assist inexperienced subcontractors if they run into major technical or quality problems.

We also feel that Government prime contractors could be greatly assisted in their efforts to subcontract high technology products to small businesses if a periodic catalog type publication existed, which details the capabilities and actual subcontract experiences and accomplishments of small businesses. As a corollary to this, prime contractors might give consideration to generating detailed subcontractor evaluation report data on past efforts with Small and Small Economically Disadvantaged Businesses. Particular emphasis would be on small companies who have succeeded in supplying parts and products to military specifications. One can conceive of distributing this information among prime contractors within the same geographic region. It would be informational as well as promotional, obviously benefitting those small businesses who have demonstrated quality performance in the past, but also challenging others to "make the list" as it were.

We believe the above points are worthy of consideration in addressing the real need of recognizing how to best interface with Small and Small Economically Disadvantaged Businesses in concert with both PL 95-507 and our continuing requirement for high technology, high quality product output to the U. S. Government. What is needed for Small Business is not more legislation, but a more practical helping hand by Government and its prime contractors so that small business can succeed in the complex world of Government and OEM business.

Sincerely,

LITTON INDUSTRIES
ELECTRON TUBE DIVISION

Gerold E. Pokorny
Manager, Electro-Optics Dept.

GEP/smt

FILIPINO CLUB of ARIZONA
1966

1981
OFFICERS

PRESIDENT
Rose Marie Dimal
VICE PRESIDENT
Chris Alcordo
SECRETARY—AUDITOR
Luxmi Cruz
TREASURER
Manet Bautista
ASSISTANT TREASURER
Clara Pontejos
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Felipe Lim, M.D.
Percy Santos
Luis Tan, M.D.
Jim Wittevrongel

TESTIMONY BEFORE THE HOUSE OF REPRESENTATIVES
COMMITTEE ON SMALL BUSINESS

PARREN J. MITCHELL, CHAIRMAN (CSB)
September 1, 1981
Phoenix, Arizona

RECEIVED
SEP 1 1981
PARREN J. MITCHELL

THIS WRITTEN TESTIMONY IS BEING SUBMITTED IN BEHALF OF THE FILIPINO COMMUNITY OF THE PHOENIX METROPOLITAN AREA AND AS A MEMBER OF THE ASIAN COALITION.

3502 E. Everett, Phoenix, AZ 85032

My name is ROSE MARIE DIMAL. I am President of the Filipino Club of Arizona which has a constituency of approximately 3,500 Filipino-Americans of good standing in this community. I am also an Asian-American and I am here to testify in behalf of the Asian Coalition--an alliance which represents the interests and general welfare of a growing community of active and truly concerned ethnic group of Americans.

My colleagues are testifying on issues of funding, procurement contracts and management development problems. Our organization would like to be on record in terms of supporting the variety of issues that representatives from the Asian Coalition have mentioned.

What I would like to address is the problem of general exclusion of Asian Americans in obtaining grants, loans, and other assistance provided by the Small Business Administration.

In as much as Asian-Americans are aware of the social service and economic purpose of the Small Business Administration, we are wondering if the encouragement of providing support for "minorities" and the "disadvantaged" have been bound by the unfair definitions of who are the minorities and who are the disadvantaged. Clearly, Asian-Americans of this country are minorities and a segment of our population are, indeed, economically and socially disadvantaged. Yet, in the implementation of the various programs under the Small Business Administration, we rarely see Asian-Americans as recipients of SBA considerations.

The Asian Coalition agrees that while we, as individual ethnic groups of Filipinos, Chinese, Koreans, Vietnamese, Japanese, and others, enjoy the positive stereotypes of being hard workers, educated, clannish, and supportive of one another--these stereotypes have been the barriers to receiving fair and equal chance of being considered for Small Business Administration benefits.

The myth needs to be dispelled: Just like any other racial and ethnic minority in this country, the Asian American communities have its poor, uneducated, jobless, socially and economically disadvantaged. We have our social problems that are unique to our cultural background, but not so unique in terms of their impact on the American society. We have constituents who wants a fair share and equal opportunity to participate in the economic development of this country by owning and operating small businesses. We have present and prospective entrepreneurs who need both direct and indirect assistance from the Small Business Administration.

In reviewing many Federally funded programs, we find that the people who are considered minorities include a whole gamut of target groups. Among those listed are Hispanics, Blacks, women in general, American Indians, juvenile delinquents, ex-offenders, physically and mentally handicapped, veterans, elderly, youth, and several others. Asians and Pacific Islanders are almost always lumped together as one category. Allocations are generally at the rate of zero up to five percent (5%) of whatever funds are being programmed; but, these allocations are rarely, if ever, subclassified into the different Asiatic and islander groupings because there simply is not enough to go around.

By the historical complacency of decision-makers, and the quiet acceptance of Asian-Americans to be treated in one minority definition, we have ignored the realistic need of this group in terms of their sub-groupings. I submit to this committee that Asian-Americans in need of SBA assistance and outreach include the Chinese, Japanese, Filipinos, Vietnamese, Koreans, Cambodians, and other Far Eastern, Oriental, and Pacific Island descents. A bigger piece of the small pie need to be extended to Asian-Americans.

Perhaps, another generalization about Asian-Americans which has caused our needs to be ignored is the notion that Asians are "new" immigrants into this country--therefore should be the last pickers of the crumbs of Federal programs. Ladies and gentlemen, Asians particularly the Chinese, Filipinos and Japanese have been in this country long before the mass migration of White Europeans in the early 1900s. Although Asians were denied American citizenship for the longest time due to discriminatory practices, Asian-Americans were among the pioneers and laborers who paved the way to progress and expansion towards the West. Asian-Americans have paid the price of coming here, of meeting the criteria of being "desirable" before actual granting of our citizenship, and of being tax-paying members of this country. Thus, in the Federal allocation of entitlements including that of the Small Business Administration, we the Asian Americans are also entitled to the benefits and considerations.

We therefore recommend that the Committee on Small Business assess and monitor SBA's policies and procedures relating to Asian-Americans' consideration for funding, procurement, management development, and other assistance. In doing so, we also recommend that advisory councils, committees, task forces and other policy-making or decision-making groups to the Small Business Administration and/or related entities include a representative(s) and/or delegate(s) from the Asian-American community. Where possible, we recommend further that at least one professional staff member of SBA offices be an Asian-American who is qualified to assist this community in meeting its needs. The Asian Coalition contends that its constituency in the general American population is significantly large enough for the Committee on Small Business to consider the above recommendations.

There is no doubt the philosophy behind the formation of the Small Business Administration is sound and commendable. The programs provided are vital to the economic empowerment of minorities. The Asian Coalition's concern is for its community to be considered fairly and equitably in the process of service delivery.

This field hearing is, indeed, a useful tool to hear the citizens' points of view, problems and concerns. Thank you for this opportunity to present our case.